EME COURT. U. S

Office-Supreme Court, U.S.
FILED
SEP 12 1968
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

Docket No. 512

GENERAL TIME CORPORATION,

Petitioner,

—against—

SECURITIES AND EXCHANGE COMMISSION, TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., and CHESTNUTT CORPORATION,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner, General Time Corporation ("General Time"), prays that a writ of certiorari issue to review the Judgment of the United States Court of Appeals for the Second Circuit entered on July 31, 1968.

Opinions Below

The opinion of the Court of Appeals is unofficially reported in CCH Fed. Sec. L. Rep. ¶92,240 (2d Cir. 1968) and is printed as Appendix A hereto.

The opinion of the United States District Court for the Southern District of New York is unofficially reported in CCH Fed. Sec. L. Rep. ¶92,224 (S. D. N. Y. 1968) and is printed as Appendix B hereto.

Jurisdiction

The Judgment of the Court of Appeals reversing the dismissal of the Complaint by the District Court was entered on July 31, 1968. The jurisdiction of this Court is invoked under Title 28, U.S.C. §1254(1).

Questions Presented

Section 17(d) of the Investment Company Act of 1940 (the "Act"), 15 U.S.C. §80a-17(d) and Rule 17d-1, 17 CFR 270.17d-1 enacted thereunder by the Securities and Exchange Commission ("SEC"), require investment companies and their statutory affiliates, as defined in §2(a)-(3) of the Act, to disclose proposed joint transactions and to seek the prior approval of the SEC, before engaging in such joint transactions. In this case, respondents, Talley Industries, Inc. ("Industries") and American Investors Fund, Inc. ("Fund"), statutory affiliates under the Act, failed to disclose and seek prior approval of their joint transaction to acquire and vote General Time stock for the purpose of enabling Industries to take over General Time. It was not until after the joint transaction had been undertaken, and Industries and Fund had each completed its acquisition of General Time stock and a proxy fight for control of General Time was being waged, that Industries and Fund filed an application for *nunc pro tunc*

approval of their joint transaction. After a full evidentiary hearing upon due notice, the SEC denied the application and held that Industries and Fund had violated the Act. The SEC subsequently filed a complaint to compel Industries and Fund, as violators of the Act, *inter alia*, to withdraw their votes cast at General Time's Annual Meeting. General Time is a defendant in that action, appeared therein and fully participated in all the proceedings in support of the relief requested in the complaint.

The District Court dismissed the complaint, but the Court of Appeals upheld the SEC determination that Industries and Fund had violated §17(d) and Rule 17d-1 and reversed the District Court. It refused, however, to direct the entry of the relief sought on the ground that such relief would not benefit Fund's stockholders, whom it held to be the sole class protected by the Act.* The questions presented are:

1. Whether the Court of Appeals improperly construed §17(d) and Rule 17d-1 when it excluded portfolio companies of investment companies and the general investing public from coverage under the protective provisions of the Act.

2. Whether the Court of Appeals, after upholding the SEC determination that §17(d) and Rule 17d-1, the important disclosure and prior approval rule of the SEC under the Act, had been violated, nullified Rule 17d-1 and abrogated the powers delegated by Congress to the SEC by improperly (a) approving, *nunc pro tunc*, the application previously rejected by the SEC, thereby substituting its judgment for that of the SEC, (b) failing to direct the entry of the only meaningful relief that would make the Rule effective and (c) permitting statutory affiliates to retain the benefits of their unlawful acts and to proceed to fruition with their unlawful takeover.

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* The Court of Appeals remanded the case to the District Court with instructions to formulate an injunction in accordance with its opinion.

Statute Involved

The relevant portions of the Investment Company Act of 1940, 15 U.S.C. §§80a-1, 80a-2(a)(3), 80a-17(d), 80a-42-(e) and Rule 17d-1 (17 CFR 270. 17d-1) thereunder are set forth in Appendix C hereto.

Statement of the Case

A. The SEC Hearing and Decision

After a full evidentiary hearing upon due notice, the SEC held in a memorandum opinion and order, dated April 19, 1968, a copy of which is printed as Appendix D hereto, that Fund and Industries secretly undertook a coordinated program "to acquire GTC [General Time] stock by concerted action" in violation of §17(d) of the Act and Rule 17d-1, with the avowed purpose of enabling Industries to take over General Time.* The SEC rejected the

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* In its opinion and order, the SEC stated as follows: "Under these circumstances, we think it clear that Industries and AIF [Fund] entered into and carried out a joint arrangement within the meaning of Section 17(d) and Rule 17d-1 to acquire GTC [General Time] stock by concerted action. The broad language of that Section and Rule indicate that the term 'joint arrangement' should not be given a narrow interpretation. Here there was not a mere happenstance of simultaneous purchases of the same security by an investment company and its affiliate. On the contrary, at Industries' instigation it and AIF undertook a coordinated program of acquisitions of the GTC stock, through a common broker, MKC [M. Kimelman & Co.], pursuant to discussions between them and agreed mechanics for its execution. Further AIF was aware of Industries' ultimate objective of bringing about a merger and was influenced to purchase GTC shares by this possibility.

"Section 17(d) and Rule 17d-1 therefore were applicable and required that an application regarding the joint arrangement be filed with and granted by us prior to the taking of any action. However, the requisite prior approval was not sought or obtained, and Industries' acquisition of GTC shares pursuant to its joint arrangement was accordingly in violation of the Act." (Appendix D, p. 49a).

belated Rule 17d-1 application of Industries and Fund, filed during the ensuing proxy fight, which sought *nunc pro tunc* approval of their joint program, and held:

> "We find no warrant for granting retroactive approval of the transactions effected in such violation. The requirement that joint arrangements and transactions by investment companies and affiliates be submitted to us for our examination before any steps are taken to carry them out is an important part of the regulatory structure which is designed to effectuate the provisions, policies and purposes of the Act. One who would ask that we disregard a failure to comply with that requirement has the burden of presenting a compelling showing that such failure was justified and that retroactive approval is not inconsistent with the statutory policies and purposes. We are unable to find that such burden has been satisfied in the present situation." (Appendix D, p. 50a).

Notwithstanding the SEC opinion and order, Fund and Industries continued their unapproved arrangement by voting those illegally acquired shares in support of Industries' takeover attempt at General Time's annual meeting which began April 22, 1968. The illegally acquired shares of either Fund or of Industries represent the swing votes in the election.

B. The SEC Suit in the District Court to Enforce Compliance with its Decision

On May 1, 1968, the SEC brought suit in the District Court to compel Industries and Fund, among other things, to withdraw their votes because they had acquired the shares so voted in violation of the Act. Voting was, and still is, an integral element in the entire unlawful joint

transaction. After trial, the District Court dismissed the complaint on the ground that the Act had not been violated. The SEC appealed and obtained a stay of the reconvened meeting and of the certification of the vote pending the outcome of the appeal. As a party to the action, supporting the relief sought, General Time also participated in the appeal proceedings, filed separate briefs and presented oral argument.

C. The Court of Appeals Opinion Denying the Relief Sought by the SEC

On July 31, 1968, the Court of Appeals reversed the dismissal of the Complaint by the District Court, and upheld the SEC finding that Industries and Fund had, indeed, violated the Act.* However, the Court of Appeals refused to direct an order against voting the stock, as sought by the SEC, on the ground that the stockholders of Fund would not benefit from such relief and that "the objective of §17(d) of the Investment Company Act is to prevent affiliated persons from injuring the interests of stockholders of registered investment companies." (Appendix A, p. 17a). By limiting the protective provisions of the Act to such stockholders and excluding therefrom portfolio companies and the investing public, the Court of Appeals has effectively and improperly nullified these important protective provisions as well as the SEC's procedure and rule duly adopted thereunder.

Reasons for Granting the Writ

A. Introduction

This case presents for the first time critical questions having broad national significance—the proper construc-

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* Reconvening the annual meeting to certify the vote has been further stayed pending formulation by the District Court of an injunction consistent with the opinion of the Court of Appeals.

tion of §17(d) of the Act and Rule 17d-1, the viability of the SEC's administrative procedures under the Act and the relief available in the face of violations of the Act. The issues presented directly affect every portfolio company of a mutual fund and, by reason thereof, the investing public and the effective regulation of the securities markets.

B. This Petition is Timely and is Filed at an Appropriate Stage in the Case

The procedural status of this case is parallel to that faced by this Court when it granted certiorari in the leading securities case of *J. I. Case Co.* v. *Borak,* 377 U. S. 426 (1964). In *Borak,* as here, the Court of Appeals reversed the District Court's dismissal of the complaint and remanded the case "to the court below for further proceedings consistent with" the opinion. (317 F. 2d 838, 849 (7th Cir. 1963)). This Court granted certiorari at that point in the proceedings to determine whether federal courts had the power to grant all necessary remedial relief for violations of the proxy rules. (377 U. S. at 428). This Court then addressed itself to the scope of relief for violation of the proxy rules and stated:

> "We, therefore, believe that under the circumstances here it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose." 377 U. S. at 433.

Likewise under the Securities Act of 1933 this Court has held, with respect to relief:

> "The power *to enforce* implies the power to make effective the right of recovery afforded by the Act. And the power to make the right of recovery effective implies the power to utilize any of the pro-

cedures or actions normally available to the litigant according to the exigencies of the particular case." *Deckert* v. *Independence Shares Corp.*, 311 U. S. 282, 288 (1940).

Here, as in *Borak* and *Deckert*, the questions of the protection and the relief available under a vital securities act are in issue. Although this Court has responded to these questions with respect to the 1933 and 1934 securities acts, it has not as yet done so under §17(d) of the 1940 Act.

In this case the Court of Appeals improperly construed the 1940 Act to the substantial detriment of portfolio companies and the investing public. As in *United States* v. *General Motors Corp.*, 323 U. S. 373, 377 (1945), the Court of Appeals' opinion poses important questions "fundamental to the further conduct of the case" which should be reviewed at this time.

C. The Court of Appeals' Construction of the Act is Inconsistent With Congressional Policy and SEC Interpretations

The Congressional concern with the dominant power of mutual funds and the peril of their expanding activities upon portfolio companies and the investing public is evident in the findings and declaration of policy of the Act. There it is recognized that "investment companies are affected with a national public interest" (§80a-1(a)) and that "such companies customarily invest and trade in securities issued by, and may dominate and control or otherwise affect the policies and management of, companies engaged in business in interstate commerce" (§80a-1(a)-(3)). The concluding paragraph of §1 of the Act states that "the purposes of this title . . . shall be interpreted . . .

to mitigate and, so far as is feasible, to eliminate the conditions enumerated in this section which adversely affect the national public interest and the interest of investors." (Appendix C, p. 40a).

The Court of Appeals concluded that "the objective of §17(d) of the Investment Company Act is to prevent affiliated persons from injuring the interests of stockholders of registered investment companies". (Appendix A, p. 17a). Certainly, while protection of investment company stockholders is one purpose of §17(d), nothing cited by the Court of Appeals or by respondents, Industries and Fund, indicates that such protection is its exclusive purpose. In addition to the policy recited in the Act itself, recent SEC pronouncements make it unmistakenly clear that the Act is also designed to protect portfolio companies against the illegal activities presented here:

> "The Act's requirements of fairness with respect to transactions between investment companies and portfolio companies in which they hold five percent or more of the outstanding voting securities gives these portfolio companies [affiliated persons] . . . *a measure of protection against overreaching by investment companies.* . . . These provisions of the Act are a check on the power of investment companies *to use their positions as large stockholders to the detriment of portfolio companies.* . . ." (Report of the Securities and Exchange Commission on the Public Policy Implications of Investment Company Growth, House Report No. 2337, 89th Cong., 2d Sess., p. 311 (1966) (Emphasis added).

That report by the SEC also stated that the

> "Act expresses concern over investment company impact . . . on companies in which investment companies are interested." (p. 27).

Moreover, the SEC in that report confirmed the Act's protection of portfolio companies when it concluded that "there is no present need for new legislation on investment company-portfolio company relationships." (pp. 27-28).

The SEC has held on other occasions (prior to and after the report referred to above) that §17 was intended to protect parties in addition to investment companies and their stockholders.

> "In our opinion, the fact that Section 17(a) by its terms makes it unlawful for the affiliate, rather than the investment company, to engage in specified types of transactions, does not, as argued by applicants, indicate a Congressional concern for the shareholders of the investment company to the exclusion of the other stockholders affected. While it is true that the protection of fund shareholders was a primary consideration which led to the passage of the Act, we find nothing in the legislative history which persuades us that Congress intended the broad language of Section 17(b) to be read in the restrictive manner which applicants suggest, nor have we ever done so." *Fifth Avenue Coach Lines, Inc.*, CCH Fed. Sec. L. Rep. Par. 77,522, p. 83,075 at 83,077 (Investment Company Act Release No. 5214, December 27, 1967). See also *Imperial Financial Services, Inc.*, CCH Fed. Sec. L. Rep. Par. 77,287 [SEC Release No. 7684, August 26, 1965].*

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* It should be noted that a §17(b) exemption for a §17(a) transaction requires a finding by the SEC that there be no overreaching whatever "on the part of any person." Thus if the fund "overreaches", the transaction cannot be exempted from §17(a). Therefore, the protections of §17 in general are not limited to merely protecting a fund, but are, by statutory mandate, broader and protect other parties.

The unregulated use in violation of the Act by a mutual fund of its substantial resources to finance its affiliate's efforts to take over a portfolio company is in direct conflict with express Congressional policy (§80a-1-(a)(2)-(5), Appendix C, pp. 39a-40a). The Court of Appeals' decision, by allowing the wrongdoers to consummate their unlawful transaction, will thwart effective SEC regulation of abuses by mutual funds.

The SEC strenuously argued in its principal brief to the Court of Appeals, dated July 9, 1968, that "disfranchisement is necessary to vindicate the broader purposes of the Act." (p. 39). The SEC reasoned:

> "The refusal of the courts to prevent the voting would tend to render meaningless the sections of the Act which require advance submission of the transaction to the Commission, since if those required to seek such advance approval are ultimately benefitted when they fail to do so, a proliferation of instances in which such requirements is ignored might be expected." (pp. 39-40).

If the SEC prayer for relief is not granted, there will be no deterrent against similar abuses in the future. Others will be encouraged, without fear of sanction, to proceed with unapproved, and therefore unlawful, joint transactions. Such a development would be inimical to the national public interest.

D. The Court of Appeals Has Improperly Substituted Its Judgment for That of the SEC and Has Abrogated Rule 17d-1

The Court of Appeals unanimously upheld the SEC's determination that Industries and Fund had, indeed, violated the Act. It recognized the applicability of the principle "that a factual determination by an agency responsi-

ble for the execution of Congressional policy and vested with expertise shall not be disturbed by a Court where there is substantial evidence to support it" (Appendix A, p. 13a). However, the Court of Appeals ignored the SEC's refusal to approve the application of Industries and Fund on a *nunc pro tunc* basis and specifically rejected the relief against voting the stock sought by the SEC, thereby permitting Fund and Industries to retain the rewards of their wrongdoing. The Court of Appeals stated that "weight must be given to the agency's selection of remedy" only where the agency petitions for "enforcement of an order making such directions" (Appendix A, p. 17a). However, the SEC, when it brought suit to enjoin Industries and Fund from voting their General Time shares, was acting to prevent participants in an unlawful joint arrangement from continuing or consummating an unlawful transaction. That action is at the very least equivalent to a finding by the SEC that such relief is required to implement the Act.

Furthermore the Court of Appeals misconstrued §42(e) of the Act and erroneously gave no weight to the SEC's decision to bring suit to enforce that agency's own formal holding that the Act had been violated.

Section 42(e) states that "upon a showing" by the SEC that a person "has engaged in or is about to engage in any act or practice constituting a violation of any provision of this title, or of any rule, regulation, or order hereunder . . . a permanent or temporary injunction or decree or restraining order shall be granted without bond." Once a violation has been shown as it has been in this case, the Court is obligated, in the absence of capriciousness and arbitrariness, to grant the injunctive relief sought by the SEC.*

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* "Failing a gross abuse of discretion, the courts should not attempt to substitute their untutored views as to what sanctions will best accord with the regulatory powers of the Commission." *Tager* v. *SEC*, 344 F. 2d 5, 9 (2d Cir. 1965).

In neither prohibiting the voting nor granting the only meaningful relief that would make the SEC rule effective, thus permitting the unlawful joint transaction in this case to continue to fruition, the Court of Appeals has effectively approved the application of Industries and Fund on a *nunc pro tunc* basis and sanctioned the takeover of General Time by an affiliate acting jointly with a registered investment company in violation of the Act.

The Court of Appeals has not only overruled the SEC, it has also refused to defer to the expertise of the SEC on matters relating to its orderly administration of its duties under the Act. Here, it has ordered the District Court to substitute its judgment for the expertise of the SEC in fashioning an injunction. And beyond that, it has, in effect, directed the District Court to confine itself merely to a consideration of the interest of stockholders of registered investment companies. This controverts the findings and declaration of policy of the Act, as stated above, and nullifies Rule 17d-1, particularly subparagraph (b) thereof, under which the SEC determined that, among the matters to be considered in passing upon applications, are the "provisions, policies and purposes of the Act."

The importance of the requirements under Rule 17d-1, which were adopted by the SEC pursuant to statutory authorization for the protection of the general investing public, has, interestingly enough, been recognized by the Court of Appeals. It states that the "only effective method of regulation [under §17(d)] was to require advance disclosure." (Appendix A, p. 16a). This is obvious because of the infinite varieties of transactions between affiliates and investment companies that should require a full disclosure and the approval of the SEC before participants

enter into a joint arrangement. See, e.g., *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U. S. 180 (1963); *SEC* v. *Texas Gulf Sulfur Co.*, CCH Fed. Sec. L. Rep. ¶ 92,251 (2d Cir. 1968). The investing public (including General Time and its stockholders) is entitled to the important benefits flowing from the application procedure, *i.e.*, advance SEC scrutiny and public disclosure and notice of joint plans of affiliates and investment companies and, as urged by the SEC, the opportunity for interested persons other than the participants to make suggestions and recommendations. Having recognized the importance of the prior disclosure and prior approval procedures, however, the Court of Appeals has effectively scuttled them by its decision.

E. The Infringement By the Court of Appeals Upon the Powers of the SEC Warrants Review by this Court

This Court has again recently demonstrated its willingness to review attempts by lower courts to infringe upon or nullify authorized administrative functions. See, *SEC* v. *New England Electric System*, 390 U. S. 207 (1968). In that case, this Court struck down a decision which "indulged in an unwarranted excursion in the administrative domain" (*Id.* at 211). The principle of that case is applicable here and warrants a grant of certiorari by this Court.

Contrary to the overly-restrictive approach of the Second Circuit, other lower federal courts have upheld the need for appropriate relief in 1940 Act cases. For example, in *SEC* v. *Quing N. Wong*, 252 F. Supp. 608 (D. P. R. 1966), the SEC sought to enjoin officers of an investment company from violating §17(d) of the Act and other securities law provisions. The relief granted included enjoining defendants from serving as officers or directors of

their investment company and other investment companies as well.

The District Court in that case held that the SEC was entitled to "complete and effective relief," including "an accounting and restitution . . . and . . . such other equitable relief as might be necessary to protect the public interest and effectuate the statutory purpose" (252 F. Supp. at 613-614).

Likewise, the First Circuit has held that when the SEC "invokes the equity powers of the Federal Court" that invocation "calls into play its inherent powers where necessary to do justice and grant full relief." *Aldred Inv. Trust* v. *SEC,* 151 F. 2d 254, 261 (1st Cir. 1945), *cert. denied,* 326 U. S. 795 (1946). Accord, *Bailey* v. *Proctor,* 160 F. 2d 78, 82 (1st Cir.), *cert. denied,* 331 U. S. 834 (1947).

If the relief sought by the SEC is not granted, Industries and Fund will realize the fruits of their wrongdoing—an unlawful takeover of General Time. But it is well-established that "an offender" against the securities laws "should not be permitted to retain the avails of his wrongdoing." *SEC* v. *Central Foundry Co.,* 167 F. Supp. 821, 827 (S. D. N. Y. 1958). "The principle is fundamental that no man shall be permitted to profit by his own wrong. It enters, by implication, into all contracts and all laws . . ." Cardozo, J., in *People* v. *Schmidt,* 216 N. Y. 324, 341, 110 N. E. 945, 950 (1915). See, II Loss, *Securities Regulation* (2d Ed. 1961), p. 957.

Meaningful relief should not be denied in this case. No principle of law requires that stockholders of a wrongdoer (Fund) should be enriched at the expense of innocent third parties. The redress of these stockholders is against the managers and officers of the Fund who violated the law. In any event, concern for Fund's stockholders should

not extend to Industries, the affiliated person, which is attempting to shield its violation behind the veil of the Fund's stockholders. *United States* v. *E. I. du Pont de Nemours & Co.*, 366 U. S. 316, 326-327 (1961); *United States* v. *Crescent Amusement Co.*, 323 U. S. 173, 189-190 (1944); *Vanadium Corp. of America* v. *Susquehanna Corp.*, 203 F. Supp. 686, 699 (D. Del. 1962). The unlawfulness of Industries' acquisition of General Time shares was made clear in the SEC opinion and order of April 19, 1968: "Industries' acquisition of GTC [General Time] shares pursuant to its joint arrangement was accordingly in violation of the Act." (Appendix D, pp. 49a-50a).

CONCLUSION

For the foregoing reasons, this Petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 573—September Term, 1967.

(Argued July 22, 1968 Decided July 31, 1968.)

Docket No. 32506

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellant,

—v.—

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION, and GENERAL TIME CORPORATION,

Defendants-Appellees.

Before:

FRIENDLY, HAYS and FEINBERG,

Circuit Judges.

Appeal by the Securities and Exchange Commission from an order of the District Court for the Southern District of New York, Inzer B. Wyatt, *Judge,* dismissing its complaint which alleged that an affiliate of a registered investment company had effected a transaction wherein the investment company was a joint or a joint and several participant, in violation of §17(d) of the Investment Company Act of 1940 and the Commission's Rule 17d-1. Reversed.

JOHN A. DUDLEY, Special Counsel (Philip A. Loomis, Jr., General Counsel, David Ferber, Solicitor, Anthony A. Vertuno, Anthony G. Gamer, Attorneys, Securities and Exchange Commission, Washington, D. C.; Mahlon M. Frankhauser, Regional Administrator, Richard V. Bandler, Associate Regional Administrator, Edwin H. Nordlinger, Attorney, New York, N. Y., of Counsel), *for Securities and Exchange Commission.*

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FRIENDLY, *Circuit Judge*:

For the second time this term, see *SEC* v. *Sterling Precision Corporation*, 393 F. 2d 214, we are confronted with a close question of interpretation of §17 of the Investment Company Act of 1940, 54 Stat. 815, setting limits on "Transactions of Certain Affiliated Persons and Underwriters."

On this occasion we believe the district judge construed the relevant clause, §17(d), too narrowly, reverse his judgment dismissing the complaint, and direct further appropriate proceedings.

I.

Section 17(d), so far as here relevant, provides as follows:

> (d) It shall be unlawful for any affiliated person of or principal underwriter for a registered investment company (other than a company of the character described in section 12(d)(3)(A) and (B)), or any affiliated person of such a person or principal underwriter, acting as principal to effect any transaction in which such registered company, or a company controlled by such registered company, is a joint or a joint and several participant with such person, principal underwriter, or affiliated person, in contravention of such rules and regulations as the Commission may prescribe for the purpose of limiting or preventing participation by such registered or controlled company on a basis different from or less advantageous than that of such other participant.

Defendant Talley Industries, Inc. (hereafter Industries) is an "affiliated person" of defendant American Investors Fund, Inc. (hereafter Fund), a registered investment company, by virtue of Fund's owning 9% of Industries' voting shares, see §2(a)(3)(B). As a result of discussions between Franz G. Talley, president of Industries, a company having a net worth of some $10 million, and Michael Kimelman, a partner in the brokerage firm of M. Kimelman & Co., in which Kimelman advanced General Time Corporation, a

much larger corporation, as a candidate for acquisition by a merger with Industries, Talley gave Kimelman an order under which he bought 24,800 shares of General Time for Industries on December 26 and 27, 1967; the price was around $23 or $24 per share. This was only some 1% of the outstanding stock of General Time, a long way from what Talley thought would be needed to afford a prospect of success if he should decide to go forward with an acquisition or merger proposal.

On December 29, 1967, Talley telephoned Fund's office, and ultimately spoke to George A. Chestnutt, Jr., president of Fund and of Chestnutt Corporation, its investment adviser. Talley told him that Industries had bought stock in a certain company which he viewed as a possible merger candidate and that he had in mind that Fund also might wish to buy some stock. Chestnutt broke off the conversation to consult his counsel. The latter advised that Fund could follow Talley's suggestion so long as it "maintained complete independence in our acquisition of stock and didn't make any promises or arrangements" as to voting, disposition or otherwise. Chestnutt relayed this to Talley, who accepted Fund's proceeding in this manner. Talley then named the company, saying he thought it a good investment that might become better under a more aggressive management. He indicated that Industries intended to buy more General Time stock in the market, with an eye toward a merger; Chestnutt got the impression that Talley was thinking of terms that would yield around $45 in Industries securities for each share of General Time. Talley proposed that Kimelman get in touch with Chestnutt; the latter, after telling Talley that 10% of the General Time stock would be his legal limit, said he would study his own data on the company, would like to see Kimelman, and would

think the whole thing over. Shortly thereafter Industries bought 42,000 shares of General Time.

Kimelman visited Chestnutt on January 3. Next day Chestnutt determined that Fund should take a position in General Time. He was motivated both by study of the company's earnings and by a belief that if Industries sought a merger, the stock would rise as a result of that offer or of others it might stimulate. On January 5 Fund placed an order with Kimelman for 205,000 shares, subsequently increased to 210,000, just under Fund's 10% limit, on a "not-held" basis, i.e., with the time of execution at the broker's discretion. Chestnutt reported this to Talley.

Chestnutt maintained close supervision of Kimelman's purchases, insisting that on days when Kimelman had "not held" orders from other customers, shares should be allocated so as not to favor another customer over Fund. Industries was also making some purchases of General Time through Kimelman but at least on one occasion agreed to forego allocation and accept the most expensive shares. By February 15 Fund had acquired 210,000 shares at an average cost of $28.49 per share.

During the first week of January 1968, Talley discussed the situation, including his initial conversation with Chestnutt, with his counsel, who did not mention §17(d). After some backing and filling unnecessary to recount, Industries resumed purchases of General Time toward the end of January. Talley talked to Chestnutt four or five times during January and reported how many shares he thought "were being acquired by the Kimelmans and himself and his friends and so on." He would give Chestnutt percentage figures of what "we have" and these rather obviously included the holdings of Fund. On February 5 Industries sold 40,000 shares to Donald Harrington, a friend of Talley's, who later increased his holdings to 104,500 shares.

Finding that the record date for General Time's annual meeting was March 1, somewhat earlier than he had believed, and that Industries' own holding were only some 52,000 shares, about 2½% of the stock as against the 10% he considered necessary for a meaningful merger proposal, Talley made a special bid on the advice of his investment bankers, Smith, Barney & Co., and against that of Chestnutt who thought this would drive the price up and would not get Industries the amount of stock it wanted. The bid, on February 19, 1968, was for 200,000 shares at 36½. General Time denounced this as "grossly inadequate" and said it had a higher offer, on a tax-free basis, from another company. Only 66,437 shares were acquired.

On the afternoon of February 19, a meeting was held at Smith, Barney & Co. at the instance of the management of General Time. Talley proposed a merger and said "We and our associates own about a third of the stock"—a figure which included Fund's holdings. Later that evening the management sent word to Talley it had decided to fight. Industries, which then owned 118,537 shares, about 5½% of the total, went back into the market and quickly bought another 139,400 shares at prices ranging from 41½ to 43½. This brought its holdings to 257,937 shares, about 12½%, at an average cost of $36.76 per share.

General Time's response was an action in the District Court for the Southern District of New York alleging *inter alia* a violation of §17(d) of the Investment Company Act and seeking an injunction against the voting of the stock, the obtaining of more, or any merger. Judge Bryan dismissed the action for lack of standing; General Time appealed. Meanwhile Industries selected ten nominees of an "Independent Stockholders Committee" for election as directors at the annual meeting of General Time on April

22, obtained a stockholders list only after litigation in Delaware, and sought to clear its proxy material with the SEC. On March 25 the SEC staff advised that the material would not be cleared unless Industries filed an application for approval of the acquisition of General Time stock by Fund and Industries under Rule 17d-1, which we reproduce in relevant part in the margin.[1] Industries filed such an application, with appropriate disclaimers of the need for

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1 Rule 17d-1. Applications Regarding Joint Enterprises or Arrangements and Certain Profit-Sharing Plans.

(a) No affiliated person of or principal underwriter for any registered investment company (other than a company of the character described in Section 12(d)(3) (A) and (B) of the Act) and no affiliated person of such a person or principal underwriter, acting as principal, shall participate in, or effect any transaction in connection with, any joint enterprise or other joint arrangement or profit-sharing plan in which any such registered company, or a company controlled by such registered company, is a participant, and which is entered into, adopted or modified subsequent to the effective date of this rule, unless an application regarding such joint enterprise, arrangement or profit-sharing plan has been filed with the Commission and has been granted by an order entered prior to the submission of such plan or modification to security holders for approval, or prior to such adoption or modification if not so submitted, except that the provisions of this rule shall not preclude any affiliated person from acting as manager of any underwriting syndicate or other group in which such registered or controlled company is a participant and receiving compensation therefor.

(b) In passing upon such application, the Commission will consider whether the participation of such registered or controlled company in such joint enterprise, joint arrangement or profit-sharing plan on the basis proposed is consistent with the provisions, policies and purposes of the Act and the extent to which such participation is on a basis different from or less advantageous than that of other participants.

(c) "Joint enterprise or other joint arrangement or profit-sharing plan" as used in this rule shall mean any written or oral plan, contract, authorization or arrangement, or any practice of understanding whereby a registered investment company or a controlled company thereof and any affiliated person of or a principal underwriter for such registered investment company, or any affiliated person of such a person or principal underwriter, have a joint or a joint and several participation or share in the profits of such enterprise or undertaking, but shall not include an investment advisory contract subject to Section 15 of the Act.

doing so; a hearing was set for April 16; and the proxy material was cleared.

General Time then started a new action in the District Court for the Southern District of New York, claiming the proxy material was false and misleading in violation of §14 of the Securities Exchange Act of 1934. Judge Tyler denied a preliminary injunction on April 11. On the next day Chestnutt was asked whether he would consider an offer for Fund's holdings in General Time from Del Coleman, president of Seeburg Corporation having its headquarters in Illinois. He countered by saying that he would be "down in front of the SEC testifying on the General Time situation next week, probably Tuesday" and might have to reveal anything that was said. Coleman first drew back but then asked whether Chestnutt would entertain a cash offer of $40 a share. Chestnutt replied that he would have to compare this with what anyone else might offer.[2]

April 13 saw the announcement of a plan to merge General Time and Seeburg Corporation, "contingent upon the continuation of General Time's present management." The details appeared on April 15. Chestnutt found the terms "shockingly unattractive"; he thought they would work out at not more than $28 per share of General Time as against a current market of $35. This, according to Chestnutt, was what made him decide to vote Fund's shares for the Committee's nominees and against the management.

The SEC hearings were held April 16, 17 and 18, oral argument was had before the Commission on April 19, and the Commission issued a Memorandum Opinion and Order

2 Chestnutt also testified that a representative of Seeburg said, "You just name a price between 35 and 50 and we will talk business." Chestnutt named no price because he didn't feel "in a position to make such an offer without talking to counsel." Counsel advised that a sale at a premium might present a problem under *Perlman* v. *Feldman*, 219 F. 2d 173 (2 Cir.), cert. denied, 349 U. S. 952 (1955).

that afternoon.[3] Concluding that Industries and Fund had entered into and carried out a joint arrangement under §17(d), that application for approval should have been made under Rule 17d-1, and that there was "no warrant for granting retroactive approval of the transactions effected in such violation," the Commission denied the application. It made no direction beyond an assertion in a footnote of its "continuing jurisdiction . . . over any future transfers by Industries of the GTC stock it has acquired . . . ."[4]

On April 22, after a further unsuccessful attempt by General Time to secure an injunction from Judge Tyler, the stockholders met, the ballots were cast, and the meeting was adjourned to May 3 so that the inspectors could count the votes and certify the result. Preliminary reports indicate a victory for Industries' slate, although by a margin considerably less than the shares voted by Fund.

On May 1, the SEC began this action in the District Court for the Southern District of New York. Asserting violation of §17(d) and Rule 17d-1 by Industries and Fund, the complaint sought temporary and permanent relief enjoining further acquisition of General Time stock, requiring Industries and Fund to withdraw any votes cast at the stockholders' meeting, enjoining the voting of such shares

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3 The opinion of the district judge states the facts as to an April 3 letter written to the Commission by the junior Senator from Illinois on stationery of the Senate Committee on Banking and Currency of which he is a member, avowedly at the instance of General Time, "an important factor in the economy of Illinois and other States, as well as a producer of essential military and other items." While we do not suppose this letter had the slightest effect, it was unnecessary, to say the least. Senators and Representatives who are importuned by constituents to engage in such epistolary efforts might do well to keep at hand Senator George Norris' classic letter of declination, quoted in Landis, The Administrative Process, 101-04 (1938).

4 Industries has filed a petition in the 9th Circuit to review this order.

for nominees proposed by Industries or for any merger with Industries, and enjoining future violations by Industries and Fund. The parties agreed that the court should order the trial to be advanced and consolidated with the hearing on the application for a preliminary injunction, see F. R. Civ. P. 65(a)(2). After trial Judge Wyatt delivered an opinion directing dismissal of the complaint, this appeal followed, and we have given it expedited treatment. Meanwhile the stockholders' meeting of General Time has been adjourned at first by stipulation and later by a stay issued by this court.

II.

The first issue is whether the SEC may lawfully conclude that when an affiliated person and a registered investment company engage in a plan to achieve together a substantial stock position in another company, they can have effected "any transaction in which such registered company . . . is a joint or a joint and several participant" with the affiliate even though there is no legally binding agreement between them; we postpone the related issue whether if that proposition be affirmed, the facts here sufficiently disclose such a plan.

Little purpose would be achieved by tired-eye scrutiny of the word "transaction." This is not a technical term; "transact" means "To prosecute negotiations; to carry on business; to have dealings . . . ." Webster's New International Dictionary (2d ed.) 2688. If any investment company and an affiliate agreed that each would buy 20% of the stock of a third company and would not sell without the other's consent, the case would evidently come within §17(d), and it would be altogether immaterial whether "transaction" was read to refer to each purchase or the

entire course of dealing or both. The real issue concerns the phrase "is a joint or a joint and several participant." [5]

We begin by conceding that, on a quick reading, such black-letter words call up an image of situations where there is a considerable degree of common understanding. Industries argues, in a conspicuously able brief, that this conclusion is reinforced by §12(a)(2) which forbids any registered investment company, in contravention of Commission rules, regulations or orders, "to participate on a joint or a joint and several basis in any trading account in securities . . . ," this rather obviously contemplating a situation where definite legal obligations are fixed. Against this, however, §17(d) must have been intended to reach situations not already covered by §12(a). Furthermore any idea that §17(d) is limited to the typical joint venture in which each of the parties has a fractional share is negated by the point that its very bite is to limit or prevent participation by the investment company "on a basis different from or less advantageous than that" of the affiliated person.

We find it hard to believe that a Congress which had declared "that the national public interest and the interest of investors are adversely affected . . . when investment companies are organized, operated, managed, or their portfolio securities are selected, in the interest of directors, officers, investment advisers, depositors, or other affiliated persons thereof . . . rather than in the interest of all

5 We thus find it unnecessary to discuss the issue, much debated by the parties, whether the SEC went beyond the statute when it added the words in Rule 17d-1(a), "in connection with, any joint enterprise or other joint arrangement or profit-sharing plan. . . ." In defining these terms subdivision (c) requires that the affiliate and the investment company "have a joint or a joint and several participation" or—not here contended—"share in the profits of such enterprise or undertaking." Hence, as to this case the critical question under the Rule is the same as under the statute.

classes of such companies' security holders," §1(b)(2), meant "a joint or a joint and several participant" to be read in light of common law concepts of jointness. The need for a liberal construction in order to effectuate the statutory purpose would be clearer if, for example, Industries had been an affiliate because of its holding of 5% or more of the voting securities of Fund, §2(a)(3)(A), rather than the reverse. Yet if "joint" embraces a loose kind of combination in cases of the former type where the case for a liberal construction is strong, as held by Judge Nordbye with respect to directors in *SEC* v. *Midwest Technical Development Corp.*, CCH Fed. Sec. L. Reptr. ¶91,252 (D. Minn. 1963), it must also do that here where the case is less so[6] —and this even though the strict letter of the statutory command is limited to the affiliate. Moreover, Congress could have thought that downstream affiliation also involved some danger that the investment company's stockholders might be put upon for the benefit of other stockholders of the affiliate.[7] "Joint" can mean not only "joined" or "united" but "combined." Webster's New International Dictionary (2d ed.) 1339. The case is thus appropriate for application

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6 *SEC* v. *Sterling Precision Corporation, supra,* 393 F. 2d 214, does not support the view that the same language can be read one way in the case of upstream and another way in the case of downstream affiliation. We there declined to expand the word "purchase" in §17(a)(2) to include a redemption by a downstream affiliate of its securities held by the investment company when a "sale" to the investment company of securities of the investment company held by an affiliate, whether downstream or upstream, admitted by the SEC to include a redemption, had been expressly excluded by Congress in §17(a)(1).

7 We have noted the Commission's Proposal, Investment Company Act Release No. 5128, Oct. 13, 1967, to modify Rule 17d-1 "to provide more precise standards for the determination whether and when an application must be filed" and in that connection to narrow the cases where application must be made. See particularly proposed paragraph (e).

of the settled principle that when administration of a statute has been confided to a regulatory agency and a statutory term is reasonably capable of the interpretation the agency has given, a court will sustain this even though it might have reached a different conclusion if the issue had arisen otherwise. *Gray* v. *Powell,* 314 U. S. 402, 411-13 (1941); *NLRB* v. *Hearst Publications, Inc.,* 322 U. S. 111, 130-32 (1944); *CIR* v. *Pepsi-Cola Niagara Bottling Corp.,* —— F. 2d ——, —— (2 Cir. 1968).

Even on that view, however, some element of "combination" is required. Industries forcefully contends this to be negated, particularly by Chestnutt's statement to Talley before Fund had even decided to make purchases of General Time. But here Industries encounters the Commission's decision to the contrary. Passing for the moment the question of the validity of the portion of Rule 17d-1 authorizing the hearing conducted by the SEC, we cannot subscribe to Industries' argument that in any event the administrative proceeding was "without legal significance," so that, as in *SEC* v. *Frank,* 388 F. 2d 486, 491 (2 Cir. 1968), the Commission was cast in the district court in the same role as a private litigant as regards factual issues. To be sure the case is not here on a petition to review the SEC's order denying Industries' application for retrospective approval, and the provision of §43(a) making its findings conclusive if supported by substantial evidence thus is not applicable by its terms. But the principle underlying that rule—that a factual determination by an agency responsible for the execution of Congressional policy and vested with expertise shall not be disturbed by a court where there is substantial evidence to support it—applies none the less, and it would be little short of absurd for us to decline to follow the same

standard by which a court reviewing the Commission's order would be bound. Cf. *SEC* v. *Central-Illinois Securities Corp.*, 338 U. S. 96, 113-27 (1949).

Our summary of the facts shows there was substantial evidence here. While no one has cast doubt on the veracity of Chestnutt's testimony as to his initial conversation with Talley, this did not preclude the Commission's drawing a contrary inference of intention from what the parties actually did. Indeed developments may well have brought Industries and Fund into a "combination" not clearly envisioned by either at the outset; war and the threat of war have always been powerful forgers of alliances. The Commission was justified in using its knowledge of the unspoken customs of the business world to conclude that, after Chestnutt had seen Industries spend over $8,300,000 in acquiring the 205,837 shares purchased in the special offer and on February 21 and 23, he was no longer a completely free agent as to the 210,000 shares Fund had purchased, on Talley's recommendation, for about 70% of that price. Experienced business men must have known at the outset that such a situation might arise. "An administrative agency with power after hearings to determine on the evidence in adversary proceedings whether violations of statutory commands have occurred may infer within the limits of the inquiry from the proven facts such conclusions as reasonably may be based upon the facts proven. One of the purposes which lead to the creation of such boards is to have decisions based on evidential facts under the particular statute made by experienced officials with an adequate appreciation of the complexities of the subject which is entrusted to their administration." *Republic Aviation* v. *NLRB*, 324 U. S. 793, 800 (1945).

III.

The other serious issue of construction is whether, in seeking to implement §17(d) by a general requirement of advance application and approval, Rule 17d-1 exceeds the authority granted by Congress. Industries contends that the power conferred by §17(d) was to prescribe *substantive* rules and regulations "for the purpose of limiting or preventing participation by such registered or controlled company on a basis different from or less advantageous than that of such other participant"; that the Commission has prescribed none but rather has unlawfully insisted on advance application and approval in every case; that the transaction thus must be deemed lawful since no valid rule or regulation prohibited it; or, at the very least, that it should be upheld because Industries did not acquire General Time stock "on a basis different from or less advantageous than that of" Fund. The issue must be considered in light of the general power conferred on the SEC by §38(a) "to make, issue, amend, and rescind such rules and regulations and such orders as are necessary or appropriate to the exercise of the powers conferred upon the Commission elsewhere in this title . . . ."[8]

Here again, while initial reaction may favor Industries' contention, reflection sustains the Commission's view. The

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8 Industries makes a point of the Commission's current effort to have Congress amend §38(a) to conform its language to that, e.g., in §20(a) of the Public Utility Holding Company Act, which empowers the SEC "to make, issue, amend, and rescind such rules and regulations and such orders as it may deem necessary or appropriate to carry out the provisions of this title . . . ." See Report of the SEC on the Policy Implications of Investment Company Growth, 89th Cong. 2d Sess., H. R. Rep. 2337, p. 343 (1966). We find it difficult to discern any truly significant difference; the Commission's purpose seems to have been to still arguments spawned by slight variations in the language of the acts it administers rather than to achieve power theretofore denied.

varieties in which participation by an investment company may be "different from or less advantageous than that" of an affiliate are infinite. The Commission could well have concluded that an attempt to specify these might fail to accomplish the Congressional purpose in some instances and in others accomplish more than Congress desired, and that the only effective method of regulation was to require advance disclosure and individual decision, at least until a pattern emerged, cf. note 7. Furthermore, as the Commission points out in brief, the public notice and opportunity for interested persons to come forward provided by the application procedure may lead to the development of significant facts that would not otherwise have been disclosed.

Industries mounts a counter-argument based on legislative history. It tells us that the Senate version of what became the Investment Company Act, S. 3580, 76th Cong. 3d Sess. (1940), included as §17(a)(4) a flat prohibition against affiliated persons' effecting transactions in which an investment company was a joint or a joint and several participant; relief would have been obtainable, as is now the case with respect to §17(a)(1), (2) and (3), by application for an exmption under §17(b). The change to the final version in which such transactions are condemned only insofar as they violate a particular standard, to be further specified in rules issued by the SEC, thus contraindicates an intention that the Commission may require advance application and approval in all instances. While this is a possible inference, it is equally likely that Congress meant only that such transactions should be governed only by the standard limned in §17(d) rather than the much more general ones of §17(b). We thus do not find the legislative history so compelling as to warrant a con-

clusion that Congress meant to deny the SEC power to utilize a method of regulation it had successfully used in other areas.

IV.

Our reversal of the judgment dismissing the complaint does not imply any belief on our part that the SEC is entitled to the drastic relief sought. Cf. *SEC* v. *Midwest Technical Development Corp., supra,* at p. 94,154. This action is not one for enforcement of an order making such directions, where weight must be given to the agency's selection of remedy. It is a suit in equity, whose essence lies in "the power of the Chancellor to do equity and mould each decree to the necessities of the particular case." *Hecht Co.* v. *Bowles,* 321 U. S. 321, 329 (1944).

The objective of §17(d) of the Investment Company Act is to prevent affiliated persons from injuring the interests of stockholders of registered investment companies by causing the company to participate "on a basis different from or less advantageous than that of such other participant." On the face of things that has not happened here up to this time, and the objective for a court of equity must be to insure that it does not happen in the future. While we do not undertake to particularize the form of a decree, a prohibition against sale of its shares by Industries without according Fund a fair opportunity to participate would be one obvious device to that end. On the other hand, as at present advised, we fail to perceive how the interest of Fund's stockholders would be advanced by such provisions as requiring Industries and Fund to withdraw votes cast at the April 22 stockholders' meeting of General Time and enjoining further voting by them. Requirements of that sort would have a strong tendency to induce forced liquidation at least on the part of Industries,

which surely did not make its large investment in order to be a voteless minority stockholder in General Time, and this might well be detrimental rather than advantageous to the stockholders of Fund. Whether or not General Time had sufficient standing to direct judicial attention to the violation of §17(d), an issue on which we have no occasion to pass, protection of the interests of its management in retention in office is not an objective of that section. While an order going beyond what would otherwise be the necessities of the case may sometimes be justified as against a deliberate flouter of regulatory statutes, Industries and Fund cannot be so regarded. Section 17(d) had been rarely construed, the only reported cases cited to us in addition to *SEC* v. *Midwest Technical Development Corp., supra,* being one portion of a decision of the Commission under the Securities Exchange Act, *Imperial Financial Services, Inc.*, Securities Act Release No. 7684 at 8-10 (1965), and a portion of a very recent case dealing primarily with §17(a), *Fifth Ave. Coach Lines, Inc.* Investment Company Act Release No. 5214, December 27, 1967. No decided case had ever applied §17(d) to a situation like that here, and conscientious counsel could well have believed the reservations Chestnutt stated were sufficient to make it inapplicable.

The judgment dismissing the complaint is reversed, with directions to the District Court to proceed promptly to formulate an injunction consistent with this opinion. The stay of the reconvening of the annual meeting of General Time will remain in effect until such injunction is issued.

Appendix B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

68 Civ. 1762

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION and GENERAL TIME CORPORATION,

Defendants.

Philip A. Loomis, Jr., General Counsel, David Ferber, Solicitor, John A. Dudley, Harold Sweetwood, Antony A. Venturo, Janet G. Gamer, Securities and Exchange Commission, Washington, D. C. for plaintiff.

(Marlon M. M. Frankhauser, Richard V. Bandler, Edwin H. Nordlieger, Securities and Exchange Commission, of Counsel.)

Donovan Leisure Newton & Irvine, by Walter L. Stratton, New York, New York, for defendant Talley Industries, Inc.

(Breck P. McAllister, Roy W. McDonald, Roger W. Kapp, Robert S. Ogden, Jr., Ben Vinar, William J. T. Brown, of Counsel.)

O'Connor & Farber, New York, New York, for defendants American Investors Fund, Inc. and Chestnutt Corporation, (Clendon H. Lee, of Counsel).

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Chadbourne, Parke, Whiteside & Wolff, New York, New York, for defendant General Time Corporation, (P. G. Pennoyer, Jr., of Counsel).

WYATT, District Judge: This is the decision after trial to the Court without a jury.

There was a motion for plaintiff Securities and Exchange Commission (SEC) for a preliminary injunction restraining in certain respects defendants Talley Industries, Inc. (Talley), American Investors Fund, Inc. (Fund) and Chestnutt Corporation. The principal relief sought by SEC was to require Talley and Fund to withdraw votes cast by them at the April 22, 1968 annual meeting of shareholders of General Time Corporation (Time).

Between December 26, 1967 and April 22, 1968, Talley bought in the open market 257,937 shares of common stock of Time; Fund in the same period bought 210,000 such shares.

The claim of SEC is that these shares were bought in violation of Section 17(d) of the Investment Company Act of 1940 (the Act; 15 U. S. C. § 80a-1 and following; Section 17(d) of the Act is 15 U. S. C. § 80a-17(d)) and of Rule 17d-1 (17 CFR § 270.17d-1) issued thereunder.

The action is brought under Section 42(e) of the Act (15 U. S. C. § 41(e) to enjoin alleged violations of that Act.

At the beginning of the hearing of the application for a preliminary injunction, the parties agreed that the Court should order the trial of the action on the merits to be advanced and consolidated with the application; this was done.

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There must be judgment for defendants.

Section 17(d) of the Act makes it unlawful for "any affiliate person of . . . a registered investment company . . . acting as principal to effect any transaction in which such registered company . . . is a joint or a joint and several participant with such person . . . in contravention of such rules and regulations as the Commission may prescribe for the purpose of limiting or preventing participation by such registered . . . company on a basis different from or less advantageous than that of such other participant."

It will be noted that conduct to be "unlawful" under Section 17(d), must be in contravention of some rule or regulation of SEC issued under the authority of Section 17(d).

The SEC has issued Rule 17d-1 (1 CFR § 270.17d-1) which reads in part as follows:

> "(a) No affiliated person of . . . any registered investment company . . . acting as principal, shall participate in, or effect any transaction in connection with, any joint enterprise or other joint arrangement or profit sharing plan in which any such registered company . . . is a participant . . . unless an application regarding such joint enterprise, arrangement or profit sharing plan has been filed with the Commission and has been granted . . . ."

The SEC has alsc in the same Rule (17 CFR § 270.17d-1 (c)) broadly defined "joint enterprise or other joint arrangement or profit-sharing plan."

It seems clear that it is within the power of the SEC to require by Regulation under Section 17(d) of the Act

that unless application in advance has been made to the SEC and granted, no affiliated person of a registered investment company acting as principal shall effect any transaction in which such registered company is a joint or a joint and several participant. On the other hand, it is also clear that by the use of such expressions as "joint enterprise or other joint arrangement or profit-sharing plan" the SEC cannot widen the reach of the statute.

The effect of the Rule 17d-1 in the case at bar, therefore, is to raise the issue of the legality of the stock purchases by Fund and by Talley.

Fund is a "registered investment company" under the Act.

Talley is an "affiliated person" of Fund because at all relevant times Fund has owned between 9% and 10% of the outstanding voting securities of Talley. 15 U. S. C. § 80a-2(a)(3)(B).

The issue in this action, therefore, is whether the purchase of Time shares by Talley or Fund or both was a "transaction" effected by Talley as "principal" in which Fund was a "joint" or joint and several participant."

Talley is a Delaware corporation with its principal office in Mesa, Arizona, some twenty miles from Phoenix. Its shares are publicly held and listed on the American Stock Exchange. Talley makes products for use as parts of jet aircraft and other space age systems and devices. Franz G. Talley (Franz) is president and the chief figure for Talley in the events in suit.

Fund is a New York corporation with its principal office in Greenwich, Connecticut. It is an investment company (a so-called "mutual fund") with assets, consisting of in-

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vestments in portfolio companies, having a market value of some 270 million dollars. George A. Chestnutt, Jr. (George) is president and the chief figure for Fund in the events in suit.

No officer or director of Fund is an officer or director of Talley and no officer or director of Talley is an officer or director of Fund. Talley owns no shares of Fund. The shares of Talley owned by Fund were bought in the open market; there have never been any transactions between Talley and Fund.

Time is also a Delaware corporation, the common stock of which is listed on the New York Stock Exchange. The principal office of Time is in Connecticut. It makes all kinds of clocks, timing devices and related equipment.

In about April 1967, Fund sent a representative to look over the Talley plant in Arizona; later in 1967 Franz and his daughter visited the Fund offices in Greenwich and had lunch with George.

Talley has been interested in acquiring other companies; it has had "a very active acquisition program" and in this connection has consulted M. Kimelman & Company (Kimelman), a brokerage firm in New York. The chief figure for Kimelman in the events in suit was Michael Kimelman (Mike), a partner.

Franz, as custodian for his two children, had an account with Kimelman.

Mike in December 1967 became interested in Time as an investment and exercising his discretion bought for the Franz custodian account on December 22, 1967, 400 shares of Time at about $23 per share.

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Franz learned of this purchase only from the confirmation slips but about the same time Mike telephoned him, discussed Time as an investment, and sent Franz a report on Time. Mike also suggested Time as a potential acquisition or merger candidate for Talley.

After studying the report, Franz gave Mike an order to buy for Talley about half to three quarter million dollars in purchase price of Time stock. Franz was seriously considering Time as a merger candidate. Mike executed the order by buying 24,800 shares on December 26 and 27, 1967.

On December 29, Franz talked to George and brought to his attention the advantages of Time as an investment for Fund, stating that Talley had bought shares of Time and that it was a possible acquisition for Talley. Undoubtedly a motive for Franz was that if acquisition or merger were attempted, shares in the hands of Fund could be presumed friendly to Talley. George broke off the conversation in order to consult counsel to Fund and did so. George then talked to Franz again and said there was no legal reason why Fund should not buy shares of Time, provided that there was no agreement with Talley as to how the shares would be voted, that Fund could dispose of its shares at any moment, that it was completely independent of Talley and had no agreement with Talley about the shares.

On January 2 and 3, 1968, Talley bought through Kimelman 42,000 shares of Time.

Franz then sent Mike to see George about January 3, 1968, and, after getting further information about Time, George decided to buy for Fund just under 10% of the outstanding shares of Time or 210,000 shares. The order

to buy was given to Kimelman on January 5. It is clear that George made an independent decision for Fund to buy these shares, believing it to be a good investment for Fund. One of the factors in his investment decision was the possibility that Talley might acquire or merge with Time. It is also clear that George made an independent decision to use Kimelman as broker, largely because Kimelman already knew of Fund's interest in Time and of Talley's interest; using Kimelman would tend to limit the knowledge in financial circles that Fund was accumulating Time stock; the more widely it was known that Fund was buying Time shares, the stronger the upward effect on share prices would be; using brokers normally employed by Fund would tend to identify Fund as buying.

Between January 5 and February 15, 1968, Kimelman bought for Fund 210,000 shares of Time at an average price of $28.49 per share.

During the same period, Talley bought 35,300 Time shares and sold 50,000 shares, one block of 10,000 shares having been sold on January 17 and 40,000 shares having been sold on February 2. The sale of 10,000 shares appears to have been made at a point when Franz was considering with counsel the possibility of offering cash or Talley stock for shares of Time; he was advised that a tax-free ruling on such an offer could not be secured if Talley itself already owned a substantial number of shares bought for cash. The sale of 40,000 shares was to a friend of Franz; in the hands of the friend, the shares would be voted as Franz wished and Talley was relieved to that extent of the investment of funds.

Thus, at the time Fund completed its purchase of 210,000 shares on February 15, Talley owned 52,100 shares.

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By this time Franz was definitely attempting to lay the foundation for an acquisition of or merger with Time. He learned that the record date for the annual meeting of stockholders of Time to be held in 1968 was March 1, 1968; this meant that more shares had to be acquired by Talley before that date.

On February 19 Talley, against the advice of George, made a "special bid" on the Stock Exchange for 200,000 Time shares at $36.50 per share. Talley bought 66,437 shares under this bid.

As a result of the special bid, the management of Time learned that Talley was accumulating Time shares.

There was a meeting on February 19 between Talley and Time people, during which Franz emphasized his interest in a "friendly merger".

On the same day, February 19, Time management issued a press release that the $36.50 Talley bid was inadequate; the price then went up, Talley obtained the 66,437 shares only, and the bid was terminated.

Later on February 19 Time management sent word to Franz that they had decided to fight Talley rather than to try to arrange a "friendly merger".

On February 21, Talley bought through Kimelman 73,200 shares in the open market and in the same fashion 66,200 shares on February 23. This completed the purchases by Talley.

Talley after February 23 owned 257,937 shares of Time bought at an average cost of $38.99 per share.

On February 24, Time commenced an action in this Court (68 Civ. 768; sometimes "the first action") against Fund,

Talley and others. The complaint averred that the purchases of Time stock by defendants had been in violation of Section 17(d) of the Act, of Section 13(a) of the Act, and of Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78a and following) and of Regulation 10b-5 issued by SEC thereunder. An injunction was asked against voting by Fund and Talley of their shares of Time, against any merger of Time and Talley, against obtaining any more shares in violation of the Act, etc.

By late February or early March 1968, Franz had determined to engage in a proxy fight for control of Time, to be determined by the election of directors of Time at the annual meeting of stockholders on April 22. Franz selected 10 nominees of an "Independent Stockholders Committee" of Time; the Committee was entirely financed by Talley and was to solicit proxies in favor of its nominees, its object being to oust the management of Time. Fund had nothing whatever to do with the decision to begin the proxy fight nor with the selection of the nominees for directors. Fund had made no commitment how it would vote its stock and was perfectly free to vote for whatever slate Fund itself decided to vote.

A list of stockholders of Time was demanded by Talley. The management of Time refused. Litigation in Delaware followed and on March 21 Talley obtained the list.

Meanwhile Talley was attempting to clear its proxy material with the SEC. Under the applicable Rules (for example, 17 CFR § 240.14a-6), proxy soliciting material must be filed with the SEC ten days before being sent to stockholders; on a showing of "good cause", however, the SEC may shorten the period (usually called, to "clear" the material), a great advantage to those soliciting.

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It is here asserted for Talley, and not denied, that on March 25 someone on the staff of SEC advised counsel for Talley that, unless an application were filed under Rule 17d-1 for approval of the purchases of Time shares by Fund and Talley, the proxy soliciting material would not be cleared by the SEC; that under such compulsion, Talley agreed to file such an application; and that thereupon the proxy soliciting material was cleared.

Thus, on March 27 Talley filed an application under Rule 17d-1 describing the purchase of Time shares by it, by Fund and by others. The application requested an order by the SEC "dismissing the Application as not encompassing transactions subject to Section 17(d) or Rule 17d-1 or, alternatively, . . . finding that the transactions hereinabove described are consistent with the provisions, policies and purposes of the Act and that the participation by the Fund therein is not on a basis different from or less advantageous than that of the other participants and granting this Application of Talley to approve such participation by it . . .". On the same day Fund joined in the application.

The following note appeared at the beginning of the application:

> "Talley Industries, Inc. disclaims that the transactions described herein are in any manner within the purview of Section 17(d) of the Investment Company Act of 1940 or any rule adopted thereunder and accordingly does not concede that the making of this Application, or a decision of the Securities and Exchange Commission with respect to the subject matter hereof, is required; nor does Talley Industries, Inc. concede that the Securities

and Exchange Commission has jurisdiction over the subject matter of this Application."

Having received the Rule 17d-1 application, the SEC on April 2 gave notice of a hearing on April 16 to consider the application.

On the next day (April 3), Senator Percy wrote to the Chairman of the SEC on stationery of the Senate Committee on Banking and Currency. This letter was inspired by the management of Time, as the Senator himself appears to concede, and was directed to the body which had just given notice of an impartial hearing on the Talley-Fund application. The letter spoke of the interest of the SEC in new legislation passed by the Senate last year to prevent "such abuses" as the "current takeover bid" by Talley. The evidence on which the Senator based his conclusion that Talley had committed an abuse was not given. Apparently the Senator was under the impression that it was part of the "tender offer situation", although Talley had made no "tender offer"; the "special bid" made on February 19 under Stock Exchange rules could scarcely be called a "tender offer". In any event, the Senator referred to the "possible utility of this case as one in which your Commission could make its attitude on and concern for these sorts of takeovers very clear to the business community". The Senator expressed himself as "gratified" that the SEC had taken note of "this serious situation" and had ordered a hearing. But the Senator was concerned that the April 22 meeting of Time would take place before the SEC could determine the issues and that if Talley won control there would be "considerable disruption". Therefore the Senator suggested that "action by your Commission in the Court to temporarily suspend

the situation and postpone the meeting would be consistent with the maintenance of your Commission's jurisdiction in the matter". Meanwhile the Senator expressed his appreciation for the "forthright action" which the SEC had already taken and his hope that SEC "will make every effort to assure that the matter is resolved in a manner which recognizes the best interests of the parties involved".

Apparently the letter of Senator Percy was hand carried to the SEC which called a session for April 4 at which counsel for Time and for Talley were present. Counsel for Time urged the SEC to bring an action in the courts against Talley and apparently there was discussion of the possibility that Time itself might bring such an action.

On the following day (April 5) the SEC indicated that it would not bring the action requested. On the same day (April 5) Time itself commenced a second action (68 Civ. 1399) in this Court. Named as defendants were Talley, Fund, the independent Stockholders Committee, and others. The charge in the complaint was that the Talley proxy soliciting material was false and misleading and therefore in violation of Section 14 of the Securities Exchange Act of 1934 (15 U.S.C. § 78a and following) and Rules of the SEC thereunder. The relief demanded was substantially the same as that sought in the first action, namely, an injunction against voting by Fund and Talley of their shares of Time, etc.

On the day the second action was commenced, an order to show cause was obtained by Time to bring on a motion for a preliminary injunction. This motion by Time was heard on April 8 by Judge Tyler, who filed on April 12 an order with opinion denying the motion. Judge Tyler

found that the materials sent out by Talley were "sufficiently exhaustive, concise, and, so far as the facts have been brought out in the preliminary hearing, true". Judge Tyler found that stockholders of Time could make an "informed choice" between the Time management and Talley.

On April 13, Time and The Seeburg Corporation announced a plan to merge Time and Seeburg "contingent upon the continuation of General Time's present management"; the terms of the proposed merger were announced.

On April 15, the SEC granted Time "leave to be heard" in the Rule 17d-1 application proceedings but denied leave to intervene.

On April 18, Judge Bryan filed an order with opinion dismissing the first action brought by Time. Judge Bryan found that Time had no standing to sue under the Act because the Act was intended to protect those having an interest in the registered investment company (Fund), specifically that Section 17(d) "was intended to protect the Fund shareholders from having their company enter into transactions with affiliates on inequitable terms". Judge Bryan rejected any claim under Rule 10b-5 because Time, the corporation, could not be injured "in a takeover situation" and that "incumbent management has no protected interest in remaining in power".

George studied the proposed Time-Seeburg merger and found it very unattractive, estimating the value given in the merger to be about $28 per Time share against a then market value of about $35 per share. George accordingly issued a statement for Fund on April 18 that he would recommend voting Fund's stock in favor of the Talley slate and the Fund directors so decided.

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The hearing before the SEC Hearing Examiner on the Rule 17d-1 application took place on April 16, 17 and 18, being concluded in the evening of April 18. Apparently having in mind the April 22 stockholders meeting of Time, the Hearing Examiner referred the matter at once to the Commission. There was oral argument before the Commission beginning at 2:30 in the afternoon of Friday, April 19. Before the argument began it was announced that a majority of the Commission had "tentatively determined" that there had been a "joint arrangement" between Talley and Fund in violation of Section 17(d) of the Act and of Rule 17d-1 and that there was no "warranty" for any retroactive approval. Counsel were advised to address themselves to "those questions". The oral argument concluded at 3:45 p.m.

The Commission at about 5:00 p.m. on the same day (April 19) made its "Memorandum Opinion and Order". It was found that the "broad language" of Section 17(d) and Rule 17d-1 indicated that the term "joint arrangement" which does not appear in the statute but only in the Rule) "should not be given a narrow interpretation". It was found that Talley and Fund had carried out a "joint arrangement" and that purchase by Talley of Time shares "pursuant to its joint arrangement was accordingly in violation of the Act". The "joint application" was denied.

There was no finding by the SEC that purchases by *Fund* were in violation of the Act. The significance of this omission will appear.

Armed with the order of the SEC, Time now made haste to this Court and in the second action appeared before Judge Tyler at ten o'clock in the morning of Monday, April 22. The Annual Meeting of Time was scheduled to

begin at two in the afternoon of that day at Stamford, Connecticut. On the basis of the SEC order, Time asked Judge Tyler to enjoin Talley from voting its shares and proxies or alternatively to adjourn the meeting. After full argument, Judge Tyler that morning declined to issue any injunction.

The meeting of stockholders of Time was duly held on April 22 and according to testimony at the trial the nominees for Talley were elected as directors of Time by some 96,000 votes.

This action was then commenced by the SEC on May 1.

The SEC allowed itself to be persuaded, unwisely as it seems to me, to throw its weight on the side of one of two contending factions in a situation where the stockholders of Time—the real parties in interest—were being given an opportunity, as Judge Tyler found, in the exercise of corporate democracy to make an "informed choice".

The wisdom of the SEC action, of course, is not one for me to decide. The sole issue is simply: did the purchases by Fund or Talley or both violate Section 17(d) of the Act?

Careful study has been given of the arguments for the SEC and for Time and no merit can be found in any of them.

Three points can be put to one side in the beginning.

First, it is not possible as a matter of law for purchases by Fund to be in violation of Section 17(d). This is because that Section only makes unlawful an activity by an "affiliated person", in this case Talley, and does not make unlawful any activity of "a registered investment

company", in this case Fund. The SEC itself appears to recognize this because its April 19 order finds only that purchases by Talley were in violation of Section 17(d) and significantly omits that purchases by Fund were in violation of the Act.

Second, Rule 17d-1 to the extent that it goes beyond Section 17(d) is invalid because without authority. Therefore, the words of the Rule, "joint enterprise or other joint arrangement or profit-sharing plan", and the definition of those words cannot serve to extend the sweep of the Act. The Rule is valid, however, if applied to a situation covered by Section 17(d).

Third, the determinations made by the SEC in its April 19 order need not be accepted by this Court. Naturally, findings of fact and conclusions of law by the able and conscientious Commissioners who acted here will be given respectful consideration, as has been done. But this is an independent civil action commenced by the SEC as a litigant in this Court, under authority of Section 42(e) of the Act (15 U. S. C. § 80a-41(e)). It is not a judicial review of an order under Section 43 of the Act (15 U.S.C. § 80a-42) and even if it were, judicial review would be meaningless if the Court were obliged to accept the determinations in the order of the SEC. The case at bar is brought under a statute virtually the same as that under which *SEC v. Frank,* 388 F. 2d 486 (2d Cir. 1968) was brought and in which Judge Friendly (at 491) said:

> "The language here, however, like that in other statutes, . . . authorizes the Commission to bring an action for an injunction 'whenever it shall appear' to it that a violation is or is about to be committed; it does not specify whether a court should give

weight to the Commission's judgment, simply stating that upon 'a proper showing' an injunction 'shall be granted.' Such bland language affords no sufficient basis for concluding that Congress meant special weight to be given the Commission's decision to allow its staff to institute suit. If Congress wishes to go further, it should say so in language all can understand."

The remaining question, decisive of the action, is whether in its purchases of Time shares, Talley "as principal" effected a "transaction" in which Fund was a "joint or joint and several participant".

That Talley, when it bought Time shares, acted "as principal" and effected a "transaction" is plain. It seems equally plain that Fund was not "a joint or a joint and several participant" with Talley in the "transaction" of purchase. Fund has no financial interest of any sort in the shares of Time bought by Talley nor any agreement, understanding or commitment of any sort ever to have any such interest. There is no conceivable way by which Fund can be in any way affected financially by the purchase by Talley of the shares.

The purchases by Talley of shares of Time were not within the language of Section 17(d) and no application to the SEC was required, or could be required by the SEC, under Rule 17d-1 or otherwise.

While this disposes of the action, a few words may be added.

Our Court of Appeals, through Judge Friendly, has not long ago spoken aptly about the Act (*Willheim* v. *Murchison*, 342 F. 2d 33, 42 (1965)):

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> "The Investment Company Act, the product of joint effort and compromise by the SEC and the industry, was drafted with a good deal of specificity; a court should give it a hospitable reception but ought not expand its words beyond their natural meaning to bring within its sweep a transaction, such as that here at issue, which is not the 'mischief and defect' aimed at by the Act and which it is doubtful that Congress would have wished to include if it had considered the problem."

The situation in the case at bar is not even remotely a "mischief and defect" at which Section 17 is aimed.

Section 17, as Judge Friendly in *Wellheim* elsewhere (at 40) pointed out, was aimed by Congress at "certain kinds of self-dealing".

The "self-dealing" at which Section 17 was aimed was that between the investment company and insiders.

The Act was passed in 1940 after a monumental study of investment companies had been made by the SEC, naturally with special emphasis on the mischiefs and defects revealed after the stock market crash in 1929. One of these, at which Section 17 was directed was described by one of the draftsmen of the Act, as follows (Jaretzki, The Investment Company Act of 1940, 26 Wash. U. L. Q. 303, 307, 317-18 (1941)):

> "Dealings *between* investment companies and affiliated persons . . . also made possible improper transactions by the unscrupulous." (emphasis added)

* * *

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> "The charge had been made that investment companies frequently were operated, not primarily in the interests of their stockholders, but in the interests of controlling groups or groups represented on the board of directors. Specifically, there have been instances of investment houses selling securities to affiliated investment companies under circumstances which at worst constituted a conscious unloading of securities on the investment company and at best a bad bargain for the investment company."

On the same subject, the SEC Report to Congress itself said (*Investment Trusts and Investment Companies*, Report of the Securities and Exchange Commission, Part Three, "Abuses and Deficiencies in the Organization and Operation of Investment Trusts and Investment Companies" 22 (1939)):

> "While the losses in a number of investment companies were attributable principally to the security market decline and general business decline, in many cases the substantial losses sustained by investment companies were the result of the numerous transactions which the sponsors, managers, officers, directors, and other controlling interests effected for their own account with the investment companies which they dominated."

The SEC has more recently described the aim of Section 17(d) as follows:

> "[R]egulate certain situations where persons making the investment decisions for the registered . . . company may have a conflict of interest and the

> danger exists that the investment company . . . may be overreached by such affiliated persons . . . ." Investment Company Act Release No. 5128 (October 13, 1967).

Judge Bryan, in dismissing the first action brought by Time in this Court, stated with specific reference to Section 17(d):

> ". . . the proscription of unapproved joint arrangements with affiliates was intended to protect the Fund shareholders from having their company enter into transactions with affiliates on inequitable terms."

When Talley bought its Time shares here, there was no possibility that Fund would be "overreached" or that "inequitable terms" would be imposed on Fund. The purchases had no financial effect on Fund and never could have. Fund had no interest of any sort in the shares bought by Talley.

True, Fund itself in separate transactions bought on its own judgment and solely for its own account 210,000 shares of Time. For all that appears, Fund made a good investment. (While irrelevant, it may be noticed that the average cost to Fund of its Time shares was $28.49 per share while the average cost to Talley was $38.99 per share.) In any event, whether Fund made a good investment or not, Section 17(d) does not apply to Fund, the "registered investment company."

What has been written above contains the findings of fact and conclusions of law required by Fed. R. Civ. P. 52(a).

The Clerk is directed to enter judgment dismissing the action as to all defendants.

So Ordered.

Appendix C

INVESTMENT COMPANY ACT OF 1940

SEC. 1.

(b) Upon the basis of facts disclosed by the record and reports of the Securities and Exchange Commission made pursuant to section 30 of the Public Utility Holding Company Act of 1935, and facts otherwise disclosed and ascertained, it is hereby declared that the national public interest and the interest of investors are adversely affected—

(1) when investors purchase, pay for, exchange, receive dividends upon, vote, refrain from voting, sell, or surrender securities issued by investment companies without adequate, accurate, and explicit information, fairly presented, concerning the character of such securities and the circumstances, policies, and financial responsibility of such companies and their management;

(2) when investment companies are organized, operated, managed, or their portfolio securities are selected, in the interest of directors, officers, investment advisers, depositors, or other affiliated persons thereof, in the interest of underwriters, brokers, or dealers, in the interest of special classes of their security holders, or in the interest of other investment companies or persons engaged in other lines of business, rather than in the interest of all classes of such companies' security holders;

(3) when investment companies issue securities containing inequitable or discriminatory provisions, or fail to protect the preferences and privileges of the holders of their outstanding securities;

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(4) when the control of investment companies is unduly concentrated through pyramiding or inequitable methods of control, or is inequitably distributed, or when investment companies are managed by irresponsible persons;

(5) when investment companies, in keeping their accounts, in maintaining reserves, and in computing their earnings and the asset value of their outstanding securities, employ unsound or misleading methods, or are not subjected to adequate independent scrutiny;

(6) when investment companies are reorganized, become inactive, or change the character of their business, or when the control or management thereof is transferred, without the consent of their security holders;

(7) when investment companies by excessive borrowing and the issuance of excessive amounts of senior securities increase unduly the speculative character of their junior securities; or

(8) when investment companies operate without adequate assets or reserves.

It is hereby declared that the policy and purposes of this title, in accordance with which the provisions of this title shall be interpreted, are to mitigate and, so far as is feasible, to eliminate the conditions enumerated in this section which adversely affect the national public interest and the interest of investors.

SEC. 2. (a) When used in this title, unless the context otherwise requires—

* * *

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(3) "Affiliated person" of another person means (A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person; (E) if such other person is an investment company, any investment adviser thereof or any member of an advisory board thereof; and (F) if such other person is an unincorporated investment company not having a board of directors, the depositor thereof.

SEC. 17.

* * *

(d) It shall be unlawful for any affiliated person of or principal underwriter for a registered investment company (other than a company of the character described in section 12 (d) (3) (A) and (B), or any affiliated person of such a person or principal underwriter, acting as principal to affect any transaction in which such registered company, or a company controlled by such registered company, is a joint or a joint and several participant with such person, principal underwriter, or affiliated person, in contravention of such rules and regulations as the Commission may prescribe for the purpose of limiting or preventing participation by such registered or controlled company on a basis different from or less advantageous than that of such other participant. Nothing contained in this subsection shall be deemed to preclude any affiliated person from acting as manager of any underwriting syndicate

or other group in which such registered or controlled company is a participant and receiving compensation therefor.

SEC. 42.

* * *

(e) Whenever it shall appear to the Commission that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this title, or of any rule, regulation, or order hereunder, it may in its discretion bring an action in the proper district court of the United States, or the proper United States court of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this title or any rule, regulation, or order hereunder. Upon a showing that such person has engaged or is about to engage in any such act or practice, a permanent or temporary injunction or decree or restraining order shall be granted without bond. In any proceeding under this subsection to enforce compliance with section 7, the court as a court of equity may, to the extent it deems necessary or appropriate, take exclusive jurisdiction and possession of the investment company or companies involved and the books, records, and assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, who with the approval of the court shall have power to dispose of any or all of such assets, subject to such terms and conditions as the court may prescribe. The Commission may transmit such evidence as may be available concerning any violation of the provisions of this title, or of any rule, regulation, or other thereunder, to the Attorney General, who, in his discretion, may institute the appropriate criminal proceedings under this title.

Appendix C

RULE 17D—1. APPLICATIONS REGARDING JOINT ENTERPRISES OR ARRANGEMENTS AND CERTAIN PROFIT-SHARING PLANS.

(*a*) No affiliated person of or principal underwriter for any registered investment company (other than a company of the chartacter described in Section 12(d) (3) (A) and (B) of the Act) and no affiliated person of such a person or principal underwriter, acting as principal, shall participate in, or effect any transaction in connection with, any joint enterprise or other joint arrangement or profit-sharing plan in which any such registered company, or a company controlled by such registered company, is a participant, and which is entered into, adopted or modified subsequent to the effective date of this rule, unless an application regarding such joint enterprise, arrangement or profit-sharing plan has been filed with the Commission and has been granted by an order entered prior to the submission of such plan or modification to security holders for approval or prior to such adoption or modification if not so submitted, except that the provisions of this rule shall not preclude any affiliated person from acting as manager of any underwriting syndicate or other group in which such registered or controlled company is a participant and receiving compensation therefor.

(*b*) In passing upon such applications, the Commission will consider whether the participation of such registered or controlled company in such joint enterprise, joint arrangement or profit-sharing plan on the basis proposed is consistent with the provisions, policies and purposes of the Act and the extent to which such participation is on a basis different from or less advantageous than that of other participants.

(*c*) "Joint enterprise or other joint arrangement or profit-sharing plan" as used in this rule shall mean any

written or oral plan, contract, authorization or arrangement, or any practice or understanding concerning an enterprise or undertaking whereby a registered investment company or a controlled company thereof and any affiliated person of or a principal underwriter for such registered investment company, or any affiliated person of such a person or principal underwriter, have a joint or a joint and several participation, or share in the profits of such enterprise or undertaking, but shall not include an investment advisory contract subject to Section 15 of the Act.

(*d*) Notwithstanding the requirements of paragraph (*a*) above, no application need be filed pursuant to this rule with respect to any of the following:

(1) Any profit-sharing plan provided by any controlled company which is not an investment company for its officers or employees, provided no affiliated person of any investment company which is an affiliated person of such controlled company participates therein.

(2) Any plan provided by any registered investment company or any controlled company for its officers or employees if such plan has been qualified under Section 401 of the Internal Revenue Code of 1954 and all contributions paid under said plan by the employer qualify as deductible under Section 404 of said Code.

(3) Any loan or advance of credit to, or acquisition of securities or other property of, a small business concern, or any agreement to do any of the foregoing, ("Investments") made by a bank and a small business investment company (SBIC) licensed under the Small Business Investment Act

of 1958, whether such transactions are contemporaneous or separated in time, where the bank is an affiliated person of either (*i*) the SBIC; or (*ii*) an affiliated person of the SBIC; but reports containing pertinent details as to investments and transactions relating thereto shall be made at such time, on such forms and by such persons as the Commission may from time to time prescribe.[1]

[1] Applicable only to small business investment companies licensed under the Small Business Investment Act of 1958.

Appendix D

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION

April 19, 1968

In the Matter of

TALLEY INDUSTRIES, INC.
3500 North Greenfield Road
Mesa, Arizona

AMERICAN INVESTORS FUND, INC.
88 Field Point Road
Greenwich, Connecticut
(812-2302)

Investment Company Act of 1940—
Section 17(d)

MEMORANDUM OPINION AND ORDER DENYING APPLICATION

American Investors Fund, Inc. ("AIF"), an open-end diversified management investment company registered under the Investment Company Act of 1940 ("Act") and Talley Industries, Inc. ("Industries"), an affiliate of AIF within the meaning of Section 2(a)(3) of the Act,[1] have

[1] Since August 8, 1967, AIF has owned more than 5 percent of the outstanding common stock of Industries.

filed a joint application for an order declaring that certain transactions described in the application including purchases of stock of General Time Corporation ("GTC") by them and certain affiliates of Industries are not subject to the provisions of Section 17(d) of the Act and Rule 17d-1 thereunder, or, in the alternative, for an order approving such transactions. After appropriate notice hearings were held at which GTC was granted leave to be heard.

At the conclusion of the applicants' presentation of their evidence in support of the application, the hearing examiner without objection referred the matter to us, and we heard oral argument by applicants and GTC. On the basis of our review we make the following findings.

Section 17(d) of the Act and Rule 17d-1 thereunder prohibit an affiliated person of an investment company, acting as principal, from participating in or effecting any transaction in connection with any joint enterprise or other joint arrangement or profit sharing plan in which any such registered company is a participant unless an application concerning such arrangement has been approved by us. The evidence adduced before the hearing examiner bearing on the issue of whether the transactions in question involved a joint arrangement within the ambit of these provisions detailed the facts surrounding those transactions. It shows that on or about December 29, 1967, Franz G. Talley, president of Industries, telephoned George A. Chestnutt, Jr., president of AIF and of Chestnutt Corporation, AIF's investment adviser, and told him that he was buying GTC stock for Industries and had in mind a possible future merger of Industries and GTC. Talley told Chestnutt that Industries had acquired and would continue to purchase GTC stock, which is listed on the New York

Stock Exchange, through the broker-dealer firm of M. Kimelman & Co., ("MKC"), and asked Chestnutt if AIF would consider buying GTC stock for its investment portfolio. Although AIF's rating of GTC stock was somewhat below the range AIF normaly considered desirable for purchase, Chestnutt felt that because of the merger possibility GTC stock had "a very good chance of going up in price" and was attractive. Chestnutt testified that he did not at that time tell Talley whether AIF would purchase any GTC stock but did state that no commitment would be made to Talley with respect to either voting or selling any stock that was purchased. He admitted, however, that he was sure that Talley considered that any GTC stock which AIF might purchase would be "in friendly hands." He acceded to Talley's request that any purchases of GTC stock be made only for AIF and not for other accounts managed by Chestnutt.

At Talley's suggestion Chestnutt met with Michael Kimelman and another partner in MKC on January 3, 1968 to discuss GTC, and the following day Chestnutt decided to purchase the stock for AIF. He then discussed with Talley the advisability of using different brokers to acquire GTC stock but, according to Chestnutt, they realized that if they did so they "might wind up bidding against each other for the same block of stock." On January 5, 1968, AIF placed an order with MKC for this purchase, at times to be determined by MKC in light of market conditions, of 205,000 shares of GTC stock, later increased to 210,000 shares. Between January 5 and February 15, 1968, MKC filled AIF's order, acquiring the 210,000 shares at an average cost of $28.49 per share. Industries acquired a net total of 257,937 shares between December 26, 1967 and February 23, 1968 at an average

cost of $36.76 per share, of which 205,837 shares were acquired following completion of AIF's acquisitions and all except 66,437 shares were acquired through MKC. During this period, Talley kept Chestnutt advised of how the stock acquisition program of Industries and Talley and his "friends" was progressing.

Under these circumstances, we think it clear that Industries and AIF entered into and carried out a joint arrangement within the meaning of Section 17(d) and Rule 17d-1 to acquire GTC stock by concerted action. The broad language of that Section and Rule indicate that the term "joint arrangement" should not be given a narrow interpretation.[2] Here there was not a mere happenstance of simultaneous purchases of the same security by an investment company and its affiliate. On the contrary, at Industries' instigation it and AIF undertook a coordinated program of acquisitions of the GTC stock, through a common broker, MKC, pursuant to discussions between them and agreed mechanics for its execution. Further AIF was aware of Industries' ultimate objective of bringing about a merger and was influenced to purchase GTC shares by this possibility.

Section 17(d) and Rule 17d-1 therefore were applicable and required that an application regarding the joint arrangement be filed with and granted by us prior to the taking of any action. However, the requisite prior approval was not sought or obtained, and Industries'

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[2] *Midwest Technical Development Corporation*, CCH Fed. Sec. L. Rep. Par. 91252 (D. Minn., July 5, 1963).

acquisition of GTC shares pursuant to its joint arrrangement was accordingly in violation of the Act.[3]

We find no warrant for granting retroactive approval of the transactions effected in such violation. The requirement that joint arrangements and transactions by investment companies and affiliates be submitted to us for our examination before any steps are taken to carry them out is an important part of the regulatory structure which is designed to effectuate the provisions, policies and purposes of the Act. One who would ask that we disregard a failure to comply with that requirement has the burden of presenting a compelling showing that such failure was justified and that retroactive approval is not inconsistent with the statutory policies and purposes. We are unable to find that such burden has been satisfied in the present situation.

Accordingly, IT IS ORDERED that the joint application of Talley Industries, Inc. and American Investors Fund, Inc. for an order declaring that certain transactions were not subject to Section 17(d) of the Investment Company Act of 1940 and Rule 17d-1 thereunder, or, in the alternative, granting approval of such transactions, be, and it hereby is, denied.

By the Commission (Commissioners Owens, Budge, Wheat, and Smith), Chairman Cohen absent and not participating.

ORVAL L. DUBOIS
Secretary

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[3] *Imperial Financial Services, Inc.*, Securities Exchange Act Release No. 7684, pp. 8-10 (August 26, 1965).

We may also note that we have continuing jurisdiction under Section 17(d) and Rule 17d-1 over any future transfers by Industries of the GTC stock it has acquired in violation of these provisions.

Appendix E

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the thirty-first day of July, one thousand nine hundred and sixty-eight.

Present:

HON. HENRY J. FRIENDLY,
HON. PAUL R. HAYS,
HON. WILFRED FEINBERG,
Circuit Judges.

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellant,

v.

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION and GENERAL TIME CORPORATION,

Defendants-Appellees.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the

Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is reversed with directions to said District Court to proceed promptly to formulate an injunction consistent with the opinion of this court.

It is further ordered, adjudged and decreed that the stay of the reconvening of the Annual Meeting of General Time Corporation shall remain in effect until such injunction is issued.

A. DANIEL FUSARO
Clerk
By: VINCENT A. CARLIN
Chief Deputy Clerk

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

Docket No. 512

GENERAL TIME CORPORATION,

Petitioner,

—against—

SECURITIES AND EXCHANGE COMMISSION, TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., and CHESTNUTT CORPORATION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF RESPONDENTS AMERICAN INVESTORS FUND, INC. AND CHESTNUTT CORPORATION IN OPPOSITION TO PETITION FOR CERTIORARI

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IN THE

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OCTOBER TERM, 1968

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GENERAL TIME CORPORATION,

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SECURITIES AND EXCHANGE COMMISSION, TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., and CHESTNUTT CORPORATION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF RESPONDENTS AMERICAN INVESTORS FUND, INC. AND CHESTNUTT CORPORATION IN OPPOSITION TO PETITION FOR CERTIORARI

Respondents American Investors Fund, Inc. (the "Fund") and Chestnutt Corporation submit this brief in opposition to the petition of General Time Corporation ("General Time") for a writ of certiorari to review the interlocutory judgment of the Court of Appeals for the Second Circuit entered on July 31, 1968 which reversed the dismissal of the SEC's complaint and remanded the case for further proceedings.

Questions Presented

1. Whether there can be any justiciable issue or any case or controversy in the Constitutional sense where

(a) The seventeen allegations of the Securities and Exchange Commission's ("SEC") complaint* allege no injury to petitioner or its shareholders.

(b) The complaint does not allege that it is on behalf of or for the benefit of petitioner or petitioner's shareholders.

(c) Petitioner's answer** in its entirety is merely an express admission of the allegations in the seventeen paragraphs of the complaint.

(d) Petitioner has made no cross-claim, no counterclaim, nor third party complaint.

(e) The SEC as sole and original plaintiff has not appealed from the District Court's final judgment on remand (entered October 4, 1968, from which final judgment General Time appealed and which appeal was argued November 1, 1968) nor petitioned for certiorari herein with respect to the interlocutory decision.

2. Whether petitioner is a real party in interest as required by Rule 17(a), F.R.Civ.P., where it does not purport to act on behalf of Fund or Fund's shareholders and neither alleges nor shows any injury to itself or its shareholders.

3. Whether it would be an improvident exercise of discretion for this Court to review a case of first impression arising under Section 17(d) of the Investment Com-

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* "Appendix A" hereto.

** "Appendix B" hereto.

pany Act of 1940* (the "Act") where there was no "deliberate flout[ing] of regulatory statutes", where "on the face of things" there had been no damage to any person or protected class, and where it appears remote that comparable or analogous situations will arise again, especially in view of the opinion by the Court of Appeals which for the first time, and clearly, has declared certain activities to be within the jurisdiction of the SEC.

4. Whether the Court of Appeals in an independent suit brought by the SEC under Section 42(e) of the Act was obliged to apply Rule 52(a), F.R.Civ.P., to the facts found by the trial judge after trial without a jury on the basis of evidence before him including oral testimony.

5. Whether the SEC could deliberately violate its own Rule 17d-1 that it *"will* consider" certain matters upon application to it, and then expressly predicate an independent action upon its own refusal to consider these same matters.

6. Whether the Court was required to allow the exact form of relief demanded in the complaint.

7. Whether a court of equity was required to decree forfeiture of voting rights now and in the future, the cancellation of votes previously cast, and the reversal of decisions taken at a shareholders' meeting where there was no deliberate flouting of the regulatory statute, where no decided case had ever applied Section 17(d) to a situation like that here, and "conscientious counsel could well have believed" that the statute was inapplicable.

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* 15 U.S.C. 80a et seq. References herein are to the Act.

8. Whether it was erroneous for the Court of Appeals to sustain the Commission's determination that Section 17(d) of the Act was applicable to the facts, passing over the District Court's contrary determination and the plain language of the statute.

9. Whether Rule 17d-1 was a valid exercise of the Commission's rule-making power, and, if valid, whether it could be applied to the facts.

Statutes Involved

The relevant portions of the Investment Company Act of 1940, 15 U. S. C. §§80a-80a-1, 80a-2(a) (3), 80a-17(d), 80a-42-(e) and Rule 17d-1 (17 CRF 270.17d-1) thereunder are set forth in "Appendix C" to the petition.

Rule 52(a), F.R.Civ.P., is as follows:

> (a) EFFECT. In all actions tried upon the facts without a jury or with an advisory jury, the court shall find the facts specially and state separately its conclusions of law thereon, and judgment shall be entered pursuant to Rule 58; and in granting or refusing interlocutory injunctions the court shall similarly set forth the findings of fact and conclusions of law which constitute the grounds of its action. Requests for findings are not necessary for purposes of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses. The findings of a master, to the extent that the court adopts them, shall be considered as the findings of the court. If an opinion or memorandum of decision is filed, it will be sufficient if the findings of fact and conclusions of law appear therein. Findings of fact and conclusions of law are unnecessary on decisions of motions under Rules 12 or 56 or any other motion except as provided in Rule 41(b).

Statement of the Case

On May 1, 1968 the SEC, in a case of first impression, complained that Talley Industries, Inc. ("Industries") and the Fund were violating Section 17(d) of the Act and Rule 17d-1 thereunder in the acquisition and voting of General Time stock, and that both such defendants had violated said Section and Rule by voting their General Time stock at its meeting held April 22, 1968, to be reconvened on May 3, 1968, when the count of votes was to be reported.

There was no claim that any person was injured or was about to be injured. The burden of the complaint* was that Industries and Fund had not obtained prior SEC approval of a joint transaction.

General Time's entire answer** consisted of an admission of the allegations of the complaint. There was no counterclaim, no crossclaim, nor any other cognizable claim by General Time.

The Commission did not allege that the action was brought on behalf of General Time or for its benefit. After an expedited trial the complaint was dismissed as to all defendants. The SEC appealed, and the Court of Appeals reversed and remanded for further proceedings on July 31, 1968, and a final judgment was entered by the District Court October 4, 1968. General Time then appealed from the final judgment on remand, but the Commission did not appeal.

The Court of Appeals heard General Time's appeal from such final judgment November 1, 1968.

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* "Appendix A" hereto.

** "Appendix B" hereto.

In the meantime, General Time on September 12, 1968, petitioned this Court for review of the July 31, 1968 interlocutory decision.

None of the real parties in interest appealed from the final judgment. None of the real parties in interest has petitioned this Court for review of the interlocutory decision.

Section 17(d) and the Rule thereunder prohibit an affiliated person of an investment company from effecting any transaction in which the affiliate and the investment company are joint participants in contravention of rules and regulations the Commission may prescribe for the purpose of limiting or preventing participation by the investment company "on a basis different from or less advantageous than" participation by the affiliate.

The Fund owns approximately 9% of Industries' stock, which made Industries an "affiliate" of the Fund, albeit a downstream affiliate. Section 2(a) 3 of the Act.

The District Court made detailed findings and concluded that there was no violation of the Act and the Rule, which it found were inapplicable. The Court of Appeals did not review the District Court's findings. It reversed and remanded, because it found that the Commission could have construed the statute as it did, and that there was sufficient evidence to support the Commission's determination. On remand the District Court entered an injunction to carry out the objective of the statute by carefully prescribing the time and manner of any sales by Industries of General Time stock, forbidding any consultation or communication between Industries and the Fund, and generally restraining any violation of the section.

While the facts are clearly stated in both opinions below, we nevertheless outline them in view of the inadequate recital in the petition.

In December, 1967, Franz G. Talley, President of Industries, told George A. Chestnutt, Jr., President of the Fund and of Chestnutt Corporation, the Fund's investment adviser, that Industries had bought stock in a certain company which Talley viewed as a possible merger candidate. Talley also said that he had in mind that the Fund might wish to buy stock in the same company. After consultation with counsel, Chestnutt reported that the Fund could follow Talley's suggestion as long as it maintained complete independence in the acquisition of stock, as to how it might vote, and in any disposition thereafter. Talley then named General Time as the Company to which he had referred. Chestnutt studied the company, and then the Fund acquired 210,000 shares of General Time stock at an average cost of $28.49 per share in January and February, 1968. The acquisition was supervised, so that broker allocation of orders could not favor customers other than the Fund, and on at least one occasion Industries agreed to forego allocation of purchases and to accept the most expensive shares.

By February 28, 1968, Industries' holdings in General Time stock aggregated 257,937 shares at an average cost of $36.76 per share. Negotiations between Talley and the management of General Time proved fruitless, and a proxy fight for control of General Time ensued.

On March 25, 1968, SEC's staff advised Industries that its proxy material would not be cleared, unless Industries filed an application for approval of the acquisition of General Time stock by the Fund and by Industries. The SEC

also requested the Fund to file an application. Industries filed such an application, in which the Fund joined, with appropriate disclaimers of the need for doing so.

Following hearings held in mid-April of 1968, the SEC issued a Memorandum Opinion and Order declaring that Industries and the Fund had entered into and carried out a joint arrangement under Section 17(d) of the Act and Rule 17d-1 which required an advance application for approval and that there was "no warrant for granting retroactive approval of the transactions effected in such violation". Accordingly, the application was denied, but no direction was given with respect to the stock acquired or the voting thereof, and the Commission merely asserted continuing jurisdiction over any disposition by Industries of its shares.

On April 22, 1968, the stockholders of General Time met and cast their ballots. The meeting was adjourned to May 3 to permit the count and the certification of the result. General Time admits Industries' slate won.

On May 1, 1968, the SEC brought suit in the District Court to enjoin Industries and the Fund, among other things, from further acquiring General Time stock and to compel each of them to withdraw the votes cast by them at the stockholders' meeting. The District Court dismissed the complaint after trial, holding the Act had not been violated.

The reversal and remand by the Court of Appeals directed further appropriate proceedings consistent with the stated legislative objective of preventing affiliated persons from injuring the interests of registered investment companies emanating from participation in transactions "on

a basis different from or less advantageous than that of such other participant". In this connection the Court noted that it failed to perceive how the interest of the Fund's stockholders would be advanced by requiring the Fund and Industries to withdraw votes cast at the stockholders' meeting, and that such relief would inflict harm, rather than prevent it. Emphasizing the power of a court of conscience to formulate a remedy suitable to specific circumstances and particular situations, the Court also concluded that the facts before it did not warrant penal sanctions such as might be called for in the case of a wilful transgression of regulatory statutes.

REASONS FOR DENYING THE WRIT

Introduction

No case or controversy is presented to this Court. Petitioner claims nothing—not even injury. There is no issue. There is no injury. There is no standing. The petition is without meaning.

No allegation of the SEC's complaint even suggested possible injury to General Time or its stockholders. General Time's answer added nothing to the complaint; it simply admitted all the allegations.

Since there was never any issue of actual or potential harm involving petitioner General Time, it was never a real party in interest. Its presence in the suit was as a nominal party only, having been named in the SEC's complaint solely to prevent the completion of General Time's annual meeting where the votes were cast by both the Fund and its downstream affiliate.

The maintenance of the status quo was not for the benefit of General Time. It was to permit a Court to determine whether shareholders of the Fund were endangered and entitled to Court protection—to see whether there was any possibility that the Fund could be injured through participation in a joint transaction on a basis "less advantageous than or different from" any participation by Industries, the Fund's statutory "affiliate"—downstream.

The District Court affirmatively found that there was ". . . no conceivable way by which Fund can be in any way affected financially by the purchase by Talley of the shares." (Pet. App., 35a)

The Court also found "It is clear that George [Chestnutt] made an independent decision for Fund to buy these shares, believing it to be a good investment for Fund." (Pet. App., 25a) See also Pet. App., 38a.

The Court of Appeals in no way disturbed these findings of the District Court. Instead, it held as a matter of law that the Commission could have construed its regulation and the statute in the manner that it did, and consequently the decision was reversed on the law. In reversing, the Court of Appeals emphasized that there had been no participation by Fund on a basis different from or less advantageous than the participation by Industries. The Court said:

> "On the face of things that has not happened here up to this time, and the objective for a court of equity must be to insure that it does not happen in the future." (Pet. App., 17a)

Thus, the Court of Appeals broadened the scope of the statute in this "close case" of first impression where "con-

scientious counsel" (Pet. App., 18a) could have advised to the contrary, and directed the District Court to enter an appropriate injunction which would prevent harm in the future, which was done October 4, 1968.

Only General Time seeks review here, but neither in its one paragraph pleading, nor anywhere else in the record, nor in its petition has it shown any possibility of past or future injury.

I.

The petition presents no justiciable issue.

No respondent had any dealings with petitioner.

Nothing in the complaint alleged injury to General Time or its shareholders.

Nothing determined by the SEC, nor by the District Court, nor by the Court of Appeals even suggests that General Time or its shareholders had been injured or could possibly be injured by any act or omission of Fund or Industries.

Consequently, there is nothing for the judicial process to act upon. No direction by this Court would confer any benefit or impose any burden upon General Time.

When General Time merely admitted the allegations in the complaint, none of which related to its legal rights or affected its business or property in any way, petitioner at the same time confessed there was no justiciable issue. No issue was adjudicated below with respect to General Time, nor could it have been.

II.

General Time is not a real party in interest and may not prosecute this petition.

The absence of any issue with respect to General Time necessarily means that no interest of General Time can be affected by this Court. Consequently, it is not a real party in interest as required by Rule 17(a), F.R.Civ.P., and it may not petition for certiorari.

III.

In the event that this Court should grant certiorari difficult questions of statutory construction and procedure would have to be determined. These questions are unlikely to recur and are of little public significance.

The immense public importance of the federal securities laws does not require that every decision thereunder should be reviewed by this Court. No matter how surprising a particular opinion may be to the parties involved, there is no occasion for this Court to speak where the unique circumstances are unlikely to recur. Indeed, since this "close question" has for the first time been resolved, all investment companies are now apprised that the Commission will claim jurisdiction where there is little more than the fortuitous investment by an investment company and an affiliate in stock of another corporation. Consequently, there is no occasion for this Court, on the basis of this case of first impression, to examine the question whether the Court of Appeals fixed the boundaries of the Commission's jurisdiction in exactly the right place. The very

fact that the decision below has been rendered by the Court which is called upon to pass upon a very large number of securities law cases makes it unlikely that the issues litigated here will again be litigated by other parties.

IV.

The decision of the District Court was not "clearly erroneous" under Rule 52(a) F.R.Civ.P.

In the event certiorari is granted, these respondents will argue here, as they did below, that the District Judge properly dismissed the complaint, and that his findings of fact were not clearly erroneous and should have been upheld. In simple terms, he found on the basis of oral testimony that there simply was no "joint transaction", and the independent acts of the Fund and Industries, each seeking its own best interests, were not subject to the Act. Moreover, the issues before the District Court were different from the issues in the proceeding on Industries' application filed with the Commission. That application related solely to the *acquisition* of stock. In contrast, the Commission's complaint in the District Court alleged the *voting* of stock to be part of the "joint transaction", and the SEC further contended that a merger was a part of the transaction. Finally, even the parties were different. Chestnutt Corporation was not a party to the proceeding before the Commission on Industries' application, in which Fund had joined.

Thus, when the Commission brought an independent action under Section 42(e) of the Act, we believe it clear that this was a proceeding *de novo,* and the District Court properly treated it as such. Consequently, it was error,

in our view, for the Court of Appeals to reject our arguments as to Rule 52(a) F.R.Civ.P., and look instead to the Commission's determination in a proceeding where the issues were different and the parties not identical. It was urged below, and these respondents would contend here, that the Court of Appeals erroneously permitted the SEC to enter the court as a contestant, and then "bootstrap" its way to an affirmance of their contentions, many of which had not been considered in the administrative proceeding where the parties were not identical.

Since all the real parties in interest, namely, the SEC, Industries and Fund, do not contest the result of the final judgment below, we do not believe that this would be an appropriate case in which to consider these intricate questions.

V.

Rule 17 d-1 is invalid as exceeding the authority of Section 17(d) of the Act and is void in its entirety.

The only authority granted by Congress was to make rules "for the purpose of limiting or preventing participation by [an investment company] on a basis different from or less advantageous than" participation by an affiliate.

The Rule purports to prohibit *all* joint transactions, unless prior approval has been obtained from the Commission, irrespective of whether there is any disadvantage or difference in the participation. Moreover, a variety of additional activities are proscribed beyond the statutory words, including any "joint arrangement", "joint enterprise", or "profit sharing plan". It is submitted that the

Rule is totally invalid as going beyond any possible interpretation of the statute and the authority granted by Congress.

VI.

The findings by both courts compelled a decision that the statute could not have been violated.

It plainly appears that Fund was able to acquire General Time's stock at an average price considerably below the average price which Industries paid. Consequently, there could not have been any violation of the statute; there was no conceivable way in which the Fund could be injured; and the dismissal of the complaint should have been affirmed.

VII.

The Commission could not predicate a suit upon its own failure to act.

The Commission had itself found no possibility of injury to the Fund, reciting the prices at which Fund purchased General Time stock and the prices at which Industries purchased such stock. Thus, the Commission was bound by its own Rule that it "*will* consider" whether any participation was "less advantageous than or different from" to grant the application, in the event that it did not dismiss the application as not required in the circumstances.

VIII.

In Answer to the Particular Points Urged by Petitioner.

(1)

The Petition Is Premature.

(Petition, pp. 7-8)

Petitioner's contention that the present case is in proper posture for review is erroneous. The Court of Appeals remanded the case to the District Court for further appropriate proceedings which have been completed since the filing of the petition herein. It did so in complete agreement with petitioner's contention that the respondent companies had failed to discover that in this "close case" Section 17(d) of the Act could be applied to the facts.

The Court of Appeals did so, also, in full awareness of the plenary power of the chancellor to do equity and to mould each decree to the necessities of the particular case. Only in the Court's refusal to presume malice and base motivation, or injury to anyone at all, did the opinion incite the petitioner's displeasure. Failure so to presume can hardly be equated with the posing of important questions "fundamental to the further conduct of the case" such as might justify interlocutory review. *U. S.* v. *General Motors Corp.*, 323 U. S. 373 (1945).

Nor is there anything in the cases cited by the petitioner which would require such a departure from regular procedure. In *J. I. Case Co.* v. *Borak*, 377 U. S. 426 (1964), the question was whether state or federal law controlled the remedy to be granted. It was there held that federal

remedies are always available to an aggrieved party for the protection of federally created rights. Indeed, the Court in *Borak* went on to hold that the particular federal remedy to be applied would have to await a trial on the merits.

Here, the federally created right of Fund shareholders has been protected after trial and after remand by a final injunction. There is no parallel between *Borak* and the the case at bar. There is no disagreement or dispute in the present case as to the extent of equitable power. The sole purported grievance of the present petitioner stems from its gratuitous assumption that the moulding process would, in some unstated manner, fall short of meeting the necessities of the case—to protect Fund shareholders.

Deckert v. *Independence Shares Corp.*, 311 U. S. 282 (1940), like *Borak,* dealt with a question as to the type of relief to be granted (i.e. legal or equitable). In that case also, the Court in holding that equitable relief was justified by the allegations of the bill, went on to state that the right to *all* of the relief prayed for was not then before it for determination.

(2)

The Court of Appeals' Statement of the Purpose of the Act Is Not Inconsistent With Congressional Policy or SEC Interpretations.

(Petition, pp. 8-11)

Although the Court of Appeals found the respondent companies in inadvertent violation of the Act, petitioner advances the argument that the Court's statement of the legislative objective was inconsistent with Congressional

policy and with SEC interpretations. Even assuming, *arguendo*, the validity of the Court's determination, it is difficult to isolate the claimed inconsistency, much less to understand it, when all sides agree that Section 17(d) of the Act aims at the prevention of injury to investment company stockholders by the actions of affiliated persons.

But, we are asked to believe nevertheless that Section 17(d) goes further; that it is designed to protect portfolio companies in the abstract, regardless of their relationship to, or whether they have "transactions" with, registered investment companies. The reason why the type of injury that might be apprehended by a portfolio company is not delineated by petitioner is that there was no "transaction" with petitioner General Time. Ownership by Fund of General Time stock is not a "transaction". Petitioner never pleaded nor claimed that ownership was a "transaction", just as petitioner never pleaded nor pointed to any injury.

Even if it could be assumed that the "protection" of portfolio companies in the abstract is an objective of Section 17(d) of the Act, nothing in this case shows any interest of petitioner which has not been protected.

(3)

The Court of Appeals Did Not Substitute Its Judgment for that of the SEC and Did Not Abrogate Rule 17d-1.

(Petition, pp. 11-14)

Again, without conceding any impropriety on the part of the respondent companies, it is certainly true that the Court of Appeals and the SEC agree that the Act was violated. The SEC besought the District Court under Section 42(e)

for a remedy in an independent suit in equity. Equitable jurisdiction having been invoked, the remedy called for the application of equitable principles. *Hecht Co.* v. *Bowles*, 321 U. S. 321, 329 (1944). It is elementary, of course, that in equity the shape of the decree is a matter of informed discretion. *Railroad Commission* v. *Pullman Co.*, 321 U. S. 496. Realizing this, the SEC as sole plaintiff never saw fit to seek interlocutory review; likewise it did not appeal the final judgment. Even less should petitioner as a nominal party be heard to complain that equity should not be done after equity has been invoked by someone else.

(4)

The Powers of the SEC Were Not Infringed by the Decision of the Court of Appeals.

(Petition, pp. 14-16)

The final footnote to the SEC's Memorandum Opinion and Order (Petition, 50a) asserts "continuing jurisdiction under Section 17(d) and Rule 17d-1 over any future transfers by Industries of the GTC stock it has acquired in violation of these provisions."

That is the only "ordering" provision by the Commission other than its denial of the application. The Court of Appeals specifically noted these provisions (Petition, 9a) and preserved intact both the denial of the application and the assertion of continuing jurisdiction.

Every power asserted by the Commission was preserved. Nothing was infringed.

Neither the Commission, nor the District Court, nor the Court of Appeals even suggests the possibility of unjust enrichment "at the expense of innocent third parties" or

the existence of "fruits of wrongdoing." (Petition, p. 15) Yet the entire petition is predicated upon these completely unsubstantiated assertions.

Since the SEC's complaint, admitted by petitioner in its entirety, contains no such allegations and there is nothing in the record remotely suggesting injury or potential injury to anyone, failure by the Commission and by two courts to find any injury is conclusive.

These arguments by petitioner are patently absurd. They emphasize that a holdover, incumbent management, admittedly voted out of office, seeks to exploit to its own ends what at most was a fortuitous and inadvertent violation of a statute, which statute and violation are wholly unrelated to the affairs of the corporation these individuals continue to manage (and its treasury to finance litigation) more than half a year after they were discharged.

No case cited by petitioner stands for the proposition that a court of equity should produce mischief, especially at the instance of a party with no interest in a proceeding. Nor is punishment and forfeiture to be countenanced in equity.

In the circumstances of this case, no warrant exists for the treatment of the respondent companies as incorrigible malefactors. As stated in *United States* v. *W. T. Grant Co.*, 345 U.S. 629, at 633:

> "The purpose of an injunction is to prevent future violations, *Swift & Co.* v. *United States,* 276 U.S. 311, 326 (1928), and, of course, it can be utilized even without a showing of past wrongs. But the moving party must satisfy the court that relief is needed. The neces-

> sary determination is that there exists some cognizable danger of recurrent violation, something more than the mere possibility which serves to keep the case alive. The chancellor's decision is based on all the circumstances; his discretion is necessarily broad and a strong showing of abuse must be made to reverse it. To be considered are the bona fides of the expressed intent to comply, the effectiveness of the discontinuance and, in some cases, the character of the past violations."

Similarly, equitable relief is denied as beyond the necessities of the case where circumstances do not amount to deliberate flouting of regulatory statutes. *S.E.C.* v. *Torr,* 87 F. 2d 446 (1937); *S.E.C.* v. *Franklin Atlas Corp.,* 154 Fed. Supp. 395 (1957).

In the *Torr* case, a temporary injunction was held to have been improvidently granted where the Court stated (p. 450):

> "It cannot be justly thought that the accused practices were commenced in disregard of the statute. They were continued for only a little over a month and only while there is evidence that it was for good cause thought that they were not in violation of the law. Until the disputed facts can be tested by a trial, the only justifiable conclusion is that the appellants were making a genuine effort to conform to the law and that negatives an inference that violations, such as they were, had been due to more than mistaken interpretation or would be persisted in after they were called in question. So far as past conduct is concerned, there was, then, no sufficient ground for the preliminary injunction, since it would not support the inference of repetition in the future. Shore v. United States (C.C.A.) 282 F. 857; Blease v. Safety Transit Co. (C.C.A.) 50 F. (2d) 852."

In the present case the Court of Appeals reversed after trial and resolved a "close question." (Petition, 2a) In reversing, the Court was especially careful that its mandate be construed in accordance with this Court's repeated expositions of traditional equity principles. The final two pages of the opinion (Petition, 17a-18a) make clear that no power of the Commission was infringed; rather equity was directed to be done.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

November, 1968

Respectfully submitted,

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Counsel for Respondents
American Investors Fund, Inc.
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STANLEY L. SABEL
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Of Counsel

APPENDIX A

Complaint

UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF NEW YORK

68 Civ. 1782

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff

—v.—

TALLEY INDUSTRIES, INC. OF ARIZONA, AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION, AND GENERAL TIME CORPORATION,

Defendants.

APPENDICES

1. It appears to the plaintiff, Securities and Exchange Commission ("Commission"), that defendants American Investors Fund, Inc. ("the Fund"), Chestnutt Corporation ("Chestnutt") and Talley Industries, Inc. ("Industries") have been and are now engaged in acts and practices which constitute violations of Section 17(d) of the Investment Company Act of 1940 ("the Act"), 15 U.S.C. 80a-17(d), and Rule 17d-1 thereunder, 17 CFR 270.17d-1. The Commission, pursuant to Section 42(e) of the Act, 15 U.S.C. 80a-41(e), brings this action to enjoin such acts and practices and for other relief.

2. This Court has jurisdiction under Section 44 of the Act, 15 U.S.C. 80a-43.

In the present case, the Court of Appeals reversed after trial and resolved a "close question." (Petition, 2a.) In reversing, the Court was especially careful that its mandate be construed in accordance with this Court's repeated expositions of traditional equity principles. The final two pages of the opinion (Petition, 17a-18a) make clear that no power of the Commission was infringed; rather equity was directed to be done.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

November, 1968

Respectfully submitted,

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APPENDIX A

Complaint

UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF NEW YORK

68 Civ. 1762

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

—v.—

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION, AND GENERAL TIME CORPORATION,

Defendants.

1. It appears to the plaintiff, Securities and Exchange Commission ("Commission"), that defendants American Investors Fund, Inc. ("the Fund"), Chestnutt Corporation ("Chestnutt") and Talley Industries, Inc. ("Industries") have been and are now engaged in acts and practices which constitute violations of Section 17(d) of the Investment Company Act of 1940 ("the Act"), 15 U.S.C. 80a-17(d), and Rule 17d-1 thereunder, 17 CFR 270.17d-1. The Commission, pursuant to Section 42(e) of the Act, 15 U.S.C. 80a-41(e), brings this action to enjoin such acts and practices and for other relief.

2. This Court has jurisdiction under Section 44 of the Act, 15 U.S.C. 80a-43.

3. Each of the defendants is an inhabitant of, transacts business in, or may be found in the Southern District of New York. The acts and transactions complained of took place in substantial part within said district.

4. Defendant Fund is a diversified open-end investment company registered under the Act.

5. Defendant Chestnutt is defendant Fund's investment adviser.

6. Defendant Industries is a corporation of which more than 5% of the outstanding voting shares are owned by the defendant Fund and have been at all times mentioned herein.

7. By reason of defendant Fund's ownership of more than 5% of the outstanding common stock of defendant Industries, Industries is an "affiliated person" of the Fund within the meaning of Section 2(a)(3) of the Act, 15 U.S.C. 80a-2(a)(3).

8. Defendant General Time Corporation ("General Time") is a corporation incorporated under the laws of the State of Delaware, having its principal place of business in the State of Connecticut. Defendant Industries owns 257,937 shares of the common stock of General Time, defendant Fund owns 210,000 shares of the common stock of General Time.

9. On or about December 29, 1967, Franz G. Talley, president of defendant Industries, advised George A. Chestnutt, Jr., president of defendant Fund and of defendant Chestnutt, that Industries was buying the stock of defen-

dant General Time with a view to Industries' effecting a merger with General Time and induced the Fund to enter into a program with Industries to purchase the common stock of General Time through a common broker, M. Kimelman & Co. ("Kimelman"), so that Industries would be in a position to effect a merger with General Time.

10. Pursuant to this program, defendant Industries acquired 257,937 shares of common stock of defendant General Time between December 26, 1967, and February 23, 1968, of which all except 66,437 shares were acquired through Kimelman; and defendant Fund acquired between January 5, 1968, and February 15, 1968, through Kimelman, 210,000 shares of common stock of General Time.

11. By reason of the acts alleged in paragraphs 9 and 10, since on or about December 29, 1967, and continuing to the date hereof, defendant Industries and defendant Fund have been engaged in a joint transaction looking toward a merger of Industries and General Time.

12. By reason of the acts alleged in paragraphs 9 and 10, since on or about December 29, 1967, and continuing to the date hereof, defendant Industries has been effecting a transaction or transactions in which defendant Fund is a joint or a joint and several participant with Industries within the meaning of Section 17(d) of the Act and in contravention of Rule 17d-1 thereunder.

13. On March 27, 1968, a joint application was filed with the Commission by defendant Industries and by defendant Fund, seeking an order declaring that certain of their activities, including those set forth in paragraph 10 hereof, were not subject to Section 17(d) of the Act or Rule 17d-1

thereunder or in the alternative, seeking approval, *inter alia,* of those transactions.

14. On April 19, 1968, the Commission, passing upon the joint application, found that the program of defendant Industries and defendant Fund constituted a joint arrangement within the meaning of Section 17(d) of the Act and Rule 17d-1 thereunder; that Industries' acquisition of the shares of defendant General Time had been in violation of the Act; and the Commission refused to grant approval of the joint arrangement. A copy of the Commission's Memorandum Opinion and Order Denying Application (Investment Company Act Release No. 5358) is attached hereto as Exhibit A and made a part hereof.

15. In connection with the Annual Meeting of Shareholders of defendant General Time, scheduled to be held on April 22, 1968, defendant Industries supported a slate of nominees for directors (the Opposition Slate) in opposition to that proposed by the management of General Time and solicited proxies in favor of the Opposition Slate.

16. The Annual Meeting of Shareholders of defendant General Time was held on April 22, 1968, and the votes of its shareholders, including the votes of defendant Industries and defendant Fund, were cast either in person or by proxy. The meeting was adjourned, to be reconvened on May 3, 1968, when the count of the inspectors is scheduled to be presented.

17. Unless restrained and enjoined defendant Industries and defendant Fund will continue to engage in the unlawful acts and practices set forth in this complaint or obtain benefits from the unlawful acts and practices in which the Commission has found that they have been engaged.

WHEREFORE, the Securities and Exchange Commission, plaintiff herein, respectfully demands:

(1) That a temporary restraining order, preliminary injunction and permanent injunction be entered restraining and enjoining defendants Industries, Fund and Chestnutt and each of them, and their directors, officers, agents, servants, employees, attorneys and those persons in active concert or participation with them from directly or indirectly acquiring, or participating in the acquisition of, any further shares of defendant General Time, or taking any other action, in any transaction in which the Fund is a joint or a joint and several participant with Industries, without first having applied to the Securities and Exchange Commission for approval of such transaction, and without such approval having first been granted by order of said Commission.

(2) That the temporary restraining order contain provisions restraining defendant General Time and its directors, officers, agents, servants, employees, attorneys and those persons in active concert or participation with it from directly or indirectly reconvening the Annual Meeting of Shareholders held on April 22, 1968, or in any manner giving effect to the votes of shareholders cast at such meeting, or holding any other meeting of shareholders of General Time until a preliminary injunction is entered.

(3) That the preliminary and permanent injunctions contain provisions

(a) requiring defendants Industries and Fund to withdraw any votes previously cast at the An-

nual Meeting of Shareholders of defendant General Time held on April 22, 1968, for shares which the Commission found Industries and Fund had acquired pursuant to a joint arrangement and enjoining Industries and Fund from voting any such shares for nominees for directors whose names have been or may be proposed directly or indirectly by or on behalf of Industries or as supporting a merger or consolidation or other combination of General Time with Industries or from voting any such shares for any merger or consolidation or other combination of General Time with Industries at any future meeting of shareholders of General Time;

(b) enjoining defendant Industries from inducing defendant Fund or any other registered investment company of which it is an affiliated person, through such company's investment adviser or otherwise, from entering into any joint transaction with Industries in violation of Section 17(d) of the Act and Rule 17d-1 thereunder;

(c) enjoining defendant Fund from entering into any other joint transaction with defendant Industries or any other affiliated person in violation of Section 17(d) of the Act and Rule 17d-1 thereunder;

(d) enjoining defendant Chestnutt from advising, aiding or abetting the defendant Fund or any other registered investment company as to which Chestnutt is an investment adviser to

engage in any joint transaction with any affiliated company in violation of Section 17(d) of the Act and Rule 17d-1 thereunder;

(c) that should the order of the Commission, dated April 19, 1968, and attached hereto, be reversed or modified, appropriate modification of the preliminary and permanent injunctions will be made.

(4) Such other and further relief as the nature of the case may require and as the Court may deem proper.

Respectfully submitted,

.....

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General Counsel

.....

DAVID FERBER
Solicitor

.....

EDWARD B. WAGNER
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.....

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May 1, 1968.

APPENDIX B

Answer of Defendant General Time Corporation

UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF NEW YORK

68 CIVIL 1762

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION, and GENERAL TIME CORPORATION,

Defendants.

Defendant General Time Corporation, by its attorneys, Chadbourne, Parke, Whiteside & Wolff, answers the complaint herein, as follows:

1. Admits each and every allegation contained in paragraphs 1 through 17 of the complaint.

WHEREFORE, defendant General Time Corporation respectfully demands that the relief prayed for in the complaint be granted.

Respectfully submitted,

CHADBOURNE, PARKE, WHITESIDE & WOLFF

BY /s/ PAUL G. PENNOYER, JR.
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A Member of the Firm
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JOHN DAVIS, CLERK

IN THE

Supreme Court of the United States

October Term, 1968

No. 512

GENERAL TIME CORPORATION,

Petitioner,

against

SECURITIES AND EXCHANGE COMMISSION, TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., and CHESTNUTT CORPORATION,

Respondents.

BRIEF OF RESPONDENT TALLEY INDUSTRIES, INC., IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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WALTER L. STRATTON,
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Of Counsel.

IN THE

Supreme Court of the United States

October Term, 1968

No. 512

GENERAL TIME CORPORATION,

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SECURITIES AND EXCHANGE COMMISSION, TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., and CHESTNUTT CORPORATION,

Respondents.

BRIEF OF RESPONDENT TALLEY INDUSTRIES, INC., IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondent Talley Industries Inc. ["Industries"] submits that the petition for writ of certiorari filed by General Time Corporation ["General Time"] should be denied because of the non-final state of the litigation below.

The decision of the Court of Appeals at issue did not finally terminate this litigation in the courts below, but merely reversed the District Court's dismissal of the plaintiff Securities and Exchange Commission's complaint, with instructions to the District Court to enter appropriate injunctive relief. Petitioner General Time, a co-defendant with respondent Industries below, does not in any way

challenge the correctness of the Court of Appeals' holding that the District Court's dismissal of the complaint should be reversed, but complains that the Court of Appeals erred in advising the District Court that relief in the form of disfranchisement of the General Time shares owned by American Investors Fund Inc. and the shares owned by Industries seemed, as the Court of Appeals was then "at present advised" (Pet. for writ of cert., Appendix A, p. 17a) inappropriate.

Since the issuance of that opinion, and since the filing of General Time's petition for certiorari directed thereto, the United States District Court for the Southern District of New York has acted in response to the mandate of the Court of Appeals below (Pet. for writ of cert., Appendix E, p. 52a) and entered a final judgment on October 4, 1968. On October 8th, petitioner filed a Notice of Appeal to the Court of Appeals from the final judgment of the District Court entered October 4th. The Court of Appeals, on October 9th, fixed dates for filing of briefs by appellant (October 18th) and by appellees (October 28th) and has set the case for argument on November 1, 1968. The Court of Appeals has stayed any action on the disputed stockholders' vote of April 22, 1968 pending determination of that appeal.

On October 9, 1968, Securities and Exchange Commission, plaintiff below and one of the respondents here, advised the Court of Appeals that the Commission will not appeal the aforesaid final judgment of the District Court.

Thus, since the entry of the non-final decision by the Court of Appeals, with its non-final suggestions as to appropriate relief, a final judgment has now been entered in the District Court and an appeal has been taken by petitioner General Time to the Court of Appeals which appeal will shortly lead to that Court's final determination on all issues, including the issues raised by the petition, i.e., issues related to relief.

We submit that it is manifestly inappropriate at this juncture for this Court to grant review of a non-final decision on an issue which is shortly due to be finally decided.

In view of the present posture of this litigation we do not address ourselves to the substantive issues raised in the petition of General Time Corporation.

CONCLUSION

General Time Corporation's petition for writ of certiorari should be denied.

Respectfully submitted,

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WALTER L. STRATTON,
BENJAMIN VINAR,
Of Counsel.

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 512

GENERAL TIME CORPORATION, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals is reported at 399 F. 2d 396. The opinion of the district court is reported at 286 F. Supp. 50.

JURISDICTION

The judgment of the court of appeals was entered on July 31, 1968. The petition for a writ of certiorari was filed on September 12, 1968. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether a company, some of whose shares have been acquired by a registered investment company in

325-725—68

conjunction with the latter's affiliate, is entitled to relief against the violation of Section 17(d) of the Investment Company Act that such acquisition involved.

2. Whether a registered investment company and its statutory affiliate, who purchased the securities of such a company in violation of Section 17(d) of the Investment Company Act and rules thereunder, should be prohibited from voting the securities to accomplish the aim of the illegal purchase.

STATUTE INVOLVED

The relevant statutory provisions, Section 17(d) of the Investment Company Act of 1940, 15 U.S.C. 80a–17(d) and Rule 17d–1 promulgated thereunder, 17 CFR 270.17d–1, are set out in Appendix C of the petition.

STATEMENT

On April 19, 1968, the Securities and Exchange Commission held in a Memorandum Opinion and Order [1] that Talley Industries, Inc. ("Talley"), an affiliated person [2] of American Investors Fund, Inc. ("the Fund") (an investment company registered under the Investment Company Act), had engaged with the Fund in a plan to acquire substantial stock of General Time Corporation ("General Time") for the purpose of facilitating Talley's goal of bringing about a merger with General Time. The Commission held that Section 17(d) of the Investment Com-

[1] *In re Talley Industries, Inc.*, Investment Company Act Release No. 5358.

[2] As that term is defined in Section 2(a)(3) of the Investment Company Act of 1940, 15 U.S.C. 80a–2(a)(3).

pany Act and Rule 17d–1 thereunder [3] were applicable to the stock purchases, and, therefore, that advance approval by the Commission should have been sought before any securities were purchased. Because the Commission found no compelling showing justifying the delay in the filing of the application, it refused retroactive approval of the joint transaction.

At General Time's annual shareholders' meeting on April 22, 1968, Talley and the Fund voted the shares of General Time stock, acquired in violation of the Act, to effectuate Talley's attempted takeover. On May 1, 1968, the Commission brought suit in the district court to enjoin future violations by Talley and the Fund and to ~~acquire~~ require them to withdraw their votes.[4] The district court dismissed the Commission's complaint on the ground that, contrary to the Com-

[3] Section 17(d) (Pet. App. 41a) makes it unlawful for a company in which a registered investment company owns five percent or more of the voting shares to act as principal in effecting any transaction in which the investment company is a joint or joint and several participant in contravention of such rules as the Commission may prescribe for the purpose of limiting or preventing participation by the investment company on a basis different from or less advantageous than that of the other participant. Rule 17d–1 generally requires that no such joint enterprise be participated in or effected until an application has been filed with and approved by the Commission.

[4] Meanwhile, the shareholders' meeting had been adjourned until May 3, 1968, at which time the official election inspectors were to report the results of the vote. The court of appeals noted in its July 31, 1968, decision that preliminary reports indicated a victory for Talley's slate (399 F. 2d at 401). The reconvening of the shareholders' meeting has been stayed or adjourned since the time the Commission instituted its action.

mission's administrative determination, Section 17(d) and Rule 17d–1 had not been violated.[5]

On July 31, 1968, the court of appeals reversed, holding that the purchases of General Time stock by Talley and the Fund constituted a joint transaction by an investment company and an affiliated person in violation of Section 17(d) of the Act and Rule 17d–1 thereunder. The court of appeals directed the district court "to proceed promptly to formulate an injunction consistent with this opinion" 399 F. 2d at 406. The mandate was transmitted to the district court on September 13, 1968. Forms of proposed judgment were submitted by the parties, including the Commission, and on October 4, 1968, the district court entered a permanent injunction, patterned to a great extent after the proposed judgment submitted by Talley.[6]

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[5] In addition to the present action commenced by the Commission, General Time, petitioner herein, brought two actions of its own in the district court seeking to prevent Talley from taking steps toward a successful takeover of General Time. The court of appeals affirmed the order of the district court which dismissed General Time's complaint under Section 17(d) of the Investment Company Act and Rule 10b–5 of the Securities Exchange Act of 1934, 17 CFR 240.10b–5. The court, in the same opinion, affirmed the district court's denial, in General Time's other action, of its motion for a preliminary injunction seeking to restrain the use of proxies allegedly obtained in violation of Rule 14a–9(a) under the Securities Exchange Act of 1934, 17 CFR 240.14a–9(a), *General Time Corporation* v. *Talley Industries, Inc., et al.*, C.A. 2, Nos. 32299, 32300, October 23, 1968. General Time has filed a petition for a writ of certiorari to review the court's denial of relief in its proxy action. See *General Time Corp.* v. *Talley Industries, Inc., et al.*, No. 716, this Term, filed November 6, 1968.

[6] The district court's Final Judgment of Permanent Injunction is set forth in the Appendix to this brief.

Briefly, the district court enjoined future violations of Section 17(d) of the Investment Company Act and Rule 17d–1 thereunder, by prohibiting Talley and the Fund (so long as Talley is an affiliated person of the Fund) from "hereafter" entering into any transaction in which Talley and the Fund are joint or joint and several participants without first having obtained the Commission's approval under Section 17(d) and Rule 17d–1.

The judgment provided (*infra*, pp. 11–12) that none of the following acts, *inter alia*, would be deemed a prohibited "transaction" (if there is no communication or consultation between Talley and the Fund): voting the shares of General Time now owned by either of them on any matter; nomination by or on behalf of Talley of directors for election to the Board of Directors of General Time; solicitation by Talley of proxies for the election of such nominees or in respect of any merger or consolidation or sale of assets involving General Time; and a merger or consolidation of General Time and Talley. The judgment specified, however, that nothing therein would affect any applications that might be required under Section 17(b) of the Act, 15 U.S.C. 80a–17(b).[7]

The judgment also provided that, so long as the Fund continues to own any General Time shares, Talley may not dispose of *its* General Time shares except on certain conditions designed to provide protection for the Fund; and that should Talley decide to dis-

[7] In the Commission's view, a proposed merger of General Time and Talley would require approval by it under that subsection.

pose of its General Time shares in a manner other than particularized in the judgment, prior approval by the Commission and thereafter by the district court would be required.

The court further ordered that the adjourned shareholders' meeting be reconvened on October 10, 1968, and that the votes cast at that earlier meeting (including the votes cast by Talley and the Fund) be counted and reported.

General Time appealed from that permanent injunction. On November 1, 1968, the court of appeals heard oral argument on the appeal. One of the issues there involved is the appropriateness of the relief granted by the district court. General Time has urged that the district court should have granted the relief requested by the Commission and that that court was required to defer to the Commission in order that the integrity of the regulatory scheme might be protected.[8]

ARGUMENT

General Time's petition seeks to have this Court pass upon questions that were not finally disposed

[8] In the proposed final judgment submitted by the Commission to the district court we had requested, among other things, that the court enjoin Talley and the Fund from taking further steps with regard to the General Time stock, including voting of the shares, unless prior approval is obtained from the Commission.

The Commission did not appeal from the judgment of the district court, even though it did not grant much of the relief the agency had sought. The Commission did, however, in response to suggestions by members of the court of appeals that the Commission's views would be welcome, file a brief with that court.

of by the judgment below but that are presented in the appeal that is presently *sub judice* before the court of appeals following the remand.[9] Accordingly, without focusing on whether the questions framed in the petition would, if presented in the proper posture, warrant review by this Court, review at this juncture should not be granted. The instant petition is in one sense premature and in another possibly academic, since it seeks review of a judgment remanding for further proceedings that have now been held and that are in the process of appellate review. Consideration by this Court of the intermediate judgment which is the subject of the present petition would not be appropriate.

Although General Time characterizes the refusal of the court of appeals in its July 31, 1968, decision to direct the district court to enter an order against voting the stock as "Denying the Relief Sought by the

[9] The court of appeals, in an intervening opinion in a related action, noted that it had, in its July 31, 1968, opinion in the instant case, already ruled "that the [district] court could not properly require Industries [Talley] and Fund to withdraw any votes cast at the stockholders' meeting or enjoin any further voting of such shares * * *" *General Time Corporation* v. *American Investors Fund, Inc.*, C.A. 2, No. 32300, October 23, 1968 (slip opinion at 116). Actually, in the opinion underlying the judgment petitioner seeks to have reviewed at this juncture, the court merely observed, after stating that it was not undertaking to particularize a decree, that "*as at present advised*, we fail to perceive how the interest of Fund's stockholders would be advanced by such provisions as requiring [Talley] and Fund to withdraw votes cast at the April 22 stockholders' meeting of General Time and enjoining further voting by them" (Pet. App. 17a) (emphasis added).

SEC" (Pet. 6), the court of appeals itself indicated that it did "not undertake to particularize the form of a decree" (399 F. 2d at 405). Indeed, General Time asserts in its pending appeal that the district court too narrowly construed the court of appeals' mandate (Brief of General Time, p. 10). Thus, while the questions presented by the petition may lurk in the opinion of the court below, we believe that they have not been squarely passed upon.

In any event, whether the court of appeals' decision of July 31, 1968, is viewed as an outright rejection of the relief requested by the Commission, as the court intimated in the intervening opinion in No. 32300 (*supra*, note 9), or is viewed as indicating the necessity for further consideration of the appropriateness of the relief to be granted, that same court is expected to clarify the issues when it disposes of the pending appeal. Indeed, should the court of appeals accept the arguments of General Time and conclude that the district court's injunction should have granted the relief requested by the Commission, the questions raised by General Time in the instant petition for a writ of certiorari would become academic. In any event, under a sound certiorari policy any consideration of the issues actually or potentially presented by this litigation should take place in the context of a concrete, final decree, and not merely on the basis of an interlocutory opinion by the court of appeals.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

PHILIP A. LOOMIS, JR.,
General Counsel,
Securities and Exchange Commission.

NOVEMBER 1968.

APPENDIX

United States District Court for the Southern District of New York

68 Civ. 1762

SECURITIES AND EXCHANGE COMMISSION, PLAINTIFF

v.

TALLEY INDUSTRIES, INC., AMERICAN INVESTORS FUND, INC., CHESTNUTT CORPORATION, AND GENERAL TIME CORPORATION, DEFENDANT

Filed October 4, 1968

FINAL JUDGMENT OF PERMANENT INJUNCTION

This matter having come on for trial before this Court without a jury, * * * and this Court having issued a final judgment and order dismissing the complaint as to all defendants; and the Court of Appeals for the Second Circuit having on July 31, 1968 issued its opinion reversing the said judgment and directing this Court to proceed promptly to formulate an injunction consistent with its opinion, and the mandate of the said Court of Appeals having been transmitted to this Court on September 13, 1968; and this Court having been advised by the Commission, by Industries, and by Fund and Chestnutt Corporation that they did not wish to present any further evidence on the subject of the relief to be granted by injunction and this Court having been advised by General Time that it wished to present further evidence on that subject

but this Court declining to receive such evidence from General Time as a nominal party defendant; and proposed forms of final judgment (with supporting memoranda) having been submitted by the Commission, by Industries, and by Fund and Chestnutt Corporation, respectively, and General Time having submitted a statement (with supporting memorandum) requesting entry of final judgment in the form proposed by the Commission; and after hearing counsel for the parties on this date,

Now, it is hereby

ORDERED, ADJUDGED AND DECREED AS FOLLOWS:

I

A. So long as, or whenever, defendant Industries is an "affiliated person" of defendant Fund as that term is defined in Section 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. § 80a–2(a)(3); the "Act"), defendants Industries and Fund are permanently enjoined from hereafter effecting any transaction in which Industries acts as principal and in which the Fund is a joint or a joint and several participant with Industries without first having obtained from the Commission approval under Section 17(d) of the Act and under Rule 17d–1 promulgated thereunder (17 CFR 270.17d–1).

B. None of the following acts is a "transaction" enjoined by paragraph A provided there is no consultation between Industries and Fund concerning the act and no communication between them concerning the act (other than that required by law or by this judgment):

1. The voting on any matter by Industries or Fund at any meeting of shareholders of General Time of any shares of common stock of General

Time ("General Time shares") now owned by either of them.

2. The nomination by or on behalf of Industries of directors for election to the Board of Directors of General Times and the solicitation by Industries, alone or in conjunction with others (not including, however, Fund) of proxies for the election of such nominees or the solicitation of proxies in respect of any merger, consolidation or sale of assets involving General Time.

3. The disposition by Fund at any time, or from time to time, of General Time shares now owned by it.

4. A merger or consolidation of General Time and Industries or any subsidiary of Industries or a sale of the assets of General Time to Industries or any subsidiary of Industries, or a sale of the assets of Industries to General Time or any subsidiary of General Time.

Nothing contained in this judgment affects whatever applications may be required under Section 17(b) of the Act.

II

So long as Industries is an "affiliated person" of Fund as that term is defined in Section 2(a)(3) of the Act, defendant Industries is permanently enjoined from entering into or inducing Fund, through its investment adviser or otherwise, to enter into any transaction in which Fund is a joint or a joint and several participant with Industries.

III

So long as Fund continues to own any of the shares of capital stock of General Time now owned by it,

defendant Industries is permanently enjoined from selling any shares of capital stock of General Time now owned by it on the New York Stock Exchange (the "Exchange") except in accordance with the following procedure: if Industries proposes to make sales of General Time stock on the Exchange, it shall notify Fund by telephone or by telegraph of the number of shares proposed to be sold; within three full business days after the giving of such notice, Fund shall notify Industries that it (Fund) does or does not propose to sell on the Exchange shares of General Time stock owned by it (Fund) within the following ten business days; if Fund notifies Industries that it (Fund) does not propose to sell any shares of General Time stock on the Exchange in that period, then Industries may sell on the Exchange its General Time shares to that number of shares stated in the notice given; if Fund notifies Industries that it (Fund) proposes to sell General Time shares on the Exchange within the following ten business days, then Industries may not sell its General Time shares on the Exchange for a period of ten business days after receipt of the notice from Fund, unless in the meantime, Fund has completed its proposed sales, as to which it shall notify Industries, or Fund shall have notified Industries that Fund had abandoned its proposal to sell General Time shares within the period. Industries shall not in any event sell on the Exchange more than 10,000 General Time shares in any five business day period nor more than 25,000 such shares in any calendar month.

IV

So long as Fund continues to own any of the shares of capital stock of General Time now owned by it, defendant Industries is permanently enjoined from hereafter disposing of General Time shares now owned

by it (Industries) except by sales on the Exchange as provided in III above and except as follows:

A. in exchange for securities of another corporation (or cash, or a combination of cash and securities) in connection with the merger, consolidation, sale of assets or liquidation of General Time, so long as such disposition by Industries is on terms and conditions available to Fund and to all other shareholders of General Time pro rata;

B. pursuant to a tender offer from any person (not an affiliated person, or an affiliated person of an affiliated person, of Industries or of the Fund), *provided* that such offer is made to Fund and to all other shareholders of General Time, and *provided further* that if any such offer is limited to a specified number of General Time shares and if the Fund shall advise Industries in writing, not later than 10 days prior to the expiration date of such offer (or not later than the expiration of one half the period of such offer if the term thereof is less than 10 days), that it desires to accept such tender offer, Industries shall take appropriate steps to give the Fund the opportunity to dispose of all of the General Time shares which Fund desires to dispose of in response to such offer, before Industries shall dispose of any of its General Time shares in response to such offer;

C. with respect to a proposed disposition by Industries of General Times shares in any other manner than one described above, Industries shall give written notice to Fund of such proposed disposition. Such notice shall include: (a) a description of each proposed transaction with the name

of each proposed purchaser from Industries, the number of shares proposed to be disposed of, the consideration to be received by Industries, the method of payment and the proposed closing date; and (b) a statement that arrangements have been made for Fund to be offered an opportunity to dispose of such number of General Time shares owned by it as is equal to the percentage of Industries' then holdings of such stock proposed to be so disposed of by Industries, such arrangements to provide for such disposition by Fund on exactly the same terms and conditions as the disposition by Industries. At the expiration of five business days after any such notice is given to Fund, Industries may proceed to dispose of the number of General Time shares set forth in the notice by it to Fund, and in the manner set forth in such notice, provided that, if within such five day period Fund elects to accept the opportunity to dispose of General Time shares on the terms specified in such notice and has so advised Industries, its (Fund's) General Time shares have been disposed of as provided in such notice; and

D. in any other manner approved by the Commission and thereafter approved by this Court.

V

Defendant Fund is enjoined promptly to notify Industries and the Commission (a) when, as and if Fund ceases to be a holder of five percent (5%) or more of Industries' outstanding voting securities and (b) when, as and if Fund ceases to be a holder of all General Time shares now owned by it.

VI

Defendant General Time is enjoined to reconvene the Annual Meeting of Shareholders of General Time, recessed from time to time since April 22, 1968, at 2 P.M. on Thursday, October 10, 1968, and to include the votes heretofore cast by Industries and Fund at the Annual Meeting of Shareholders of General Time held on April 22, 1968 in the count of votes cast at the meeting, and to require the inspectors of the election of directors of General Time to report on the results of the voting at the aforementioned Annual Meeting and to complete the business at said Annual Meeting in accordance with the By-laws of General Time and in accordance with its normal practice.

VII

This action is dismissed as to defendant Chestnutt Corporation.

VIII

Jurisdiction is retained by this Court for the purpose of enabling any party to apply at any time to this Court for such further order and directions as may be necessary or appropriate for the construction or carrying out of this Final Judgment, for the modification or termination of any provisions hereof, for the enforcement of compliance herewith or for the punishment of violations hereof.

Dated: New York, New York
October 4, 1968

INZER B. WYATT,
United States District Judge.

Judgment entered:

_____ _____,
Clerk.

U.S. GOVERNMENT PRINTING OFFICE: 1968